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Executive Summary

1. On 27 October 2009, the Government published a consultation paper reviewing the regulation of credit and store cards. The purpose of this consultation was to secure a better deal for consumers, giving them improved control of their credit and store card borrowing, whilst also ensuring that any intervention is proportionate, transparent and targeted. The consultation document (including a plain English version), this Government response (and its plain English version) and the final economic and equality impact assessments are available at www.bis.gov.uk/creditconsultation/response. This document is the summary of responses to the consultation on the review of the regulation of credit and store cards.

2. In our consultation document we identified four specific areas of credit and store cards where we thought a review of existing market practices was necessary. These were firstly, the requirement that repayments to a credit or store card are allocated to debts attracting the highest interest rates first; secondly, the level of minimum payments; thirdly, the issue of unsolicited credit limits; and finally, the ability of lenders to raise interest rates on existing debts. The consultation document also identified scope to improve the simplicity and transparency of credit and store cards more generally.

3. In light of the responses received to our consultation and further evidence gathered during the consultation period, the Government has announced five new consumer rights which we believe give consumers a fairer deal and more control over the way in which they can choose and use their credit and store cards. A number of these consumer rights are targeted specifically at helping more financially vulnerable consumers. These rights are:

- **Right to repay:** consumers’ repayments will always be put against the highest rate debt first. For consumers opening new accounts the minimum payment will always cover at least interest, fees and charges, plus 1% of the principal to encourage better repayment practice.
- **Right to control:** consumers will have the right to choose not to receive credit limit increases in future and the right to reduce their limit at any time; and consumers will have better automated payment options. Consumers will have access to these options online.
- **Right to reject:** consumers will be given more time to reject increases in their interest rate or their credit limit.
- **Right to information:** consumers at risk of financial difficulties will be given guidance on the consequences of paying back too little. Consumers will be given clear information on increases in their interest rate or their credit limit, including the right to reject.
- **Right to compare:** consumers will have an annual statement that allows for easy cost comparison with other providers.

The detail of these new consumer rights is set out in the Executive Summary of the Government response which can be found at www.bis.gov.uk/creditconsultation/response.
4. This summary of responses sets out the views of respondents to the consultation in each of the five areas covered by the consultation document.
The Consultation Process

5. The consultation was conducted between 27 October 2009 and 19 January 2010. The consultation asked 80 questions covering a range of issues. The consultation questions are attached at Annex A.

6. The consultation launch was supported by a press notice, coverage in most national and regional newspapers and a publicity campaign which included GMTV, BBC Breakfast, Today programme, BBC News 24, ITN (National and Regional), Sky and a number of radio interviews. During the consultation period, the Minister for Consumer Affairs, Kevin Brennan MP, also did a podcast with FT.Online and a live webchat on the Number 10 website.

7. Copies of the consultation document and the draft economic and equality impact assessments were sent to key stakeholders, placed onto the Department for Business, Innovation and Skills (BIS) website at www.bis.gov.uk/creditconsultation and hardcopies were made available via the BIS Publications Orderline. In addition, BIS worked with Simply Understand to create a plain English version and an audio summary of the consultation, both of which were also available on the BIS website. We also worked closely with a range of key interested stakeholders to publicise the consultation through internal company intranets / conferences and /or email newsletters.

8. Over the period of the consultation, 3950 respondents voted in our online poll (see Figure 1 for results), 742 respondents left comments on our website and 204 commented directly via our dedicated email address cscr@bis.gov.uk. These comments have been analysed by BIS officials and have been taken into account in our Government response. Some of the comments and observations made have also been quoted in this document as representative of the thoughts and views coming from consumers.

9. In addition, we are aware of many comments on other websites and forums, including the BBC Have your Say webpage, www.moneysupermarket.com and www.Moneysavingexpert. The comments made on these external forums were similar in nature and tone to those that were made on our website and by email. Whilst the comments made on these external websites are not official responses to our consultation, they have also been considered by BIS officials, and have helped inform the Government response to the consultation. Where appropriate and relevant, some of the comments made have been quoted in this summary of responses document.

10. A total of 35 formal responses to the consultation were received. Figure 2 shows a breakdown of responses by sector. A list of those respondents who did not request confidentiality can be found at Annex B.

11. To supplement the consultation process, the Minister for Consumer Affairs held a series of meetings with a number of relevant organisations. BIS officials also attended a number of committee meetings and workshops, as well as holding a series of meetings on an individual basis with industry participants. A list of those organisations we met with can be found at Annex C. The points
raised in these meetings have been taken into account in the Government response to the consultation.

12. To help inform the Government’s response, BIS also commissioned two research projects late last year and the findings of both have been taken into account in this response. One of these conducted a consumer survey, and also involved a number of focus groups to explore consumer attitudes and behaviour in greater depth. The other research project looked at international experience of credit card regulation, including the recent US CARD Act. The results of both research projects are available at www.bis.gov.uk/creditconsultation/response.

13. The Government is grateful for all the consultation responses received and all the comments made both directly to BIS and on forums. This paper seeks to reflect the views offered, although it is not possible to describe all the responses in detail.

**Figure 1 – Results of online poll: most important issues for consumers**

The question asked read: “The Government wants to secure a better deal for consumers, giving you better control of your credit and store card borrowing, whilst ensuring that any regulation is proportionate, transparent and targeted. We are consulting on changes to credit card and store cards. Which of the following is the biggest issue for you?”

<table>
<thead>
<tr>
<th>Issue</th>
<th>Votes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Allocation of payments</td>
<td>1423</td>
</tr>
<tr>
<td>Minimum repayments</td>
<td>519</td>
</tr>
<tr>
<td>Unsolicited credit increases</td>
<td>457</td>
</tr>
<tr>
<td>Re-pricing of existing debts</td>
<td>802</td>
</tr>
<tr>
<td>Simplicity and transparency</td>
<td>749</td>
</tr>
</tbody>
</table>

**Total voters** 3950

![Results of online poll](image)
### Figure 2 - Responses from organisations by sector

<table>
<thead>
<tr>
<th>Sector</th>
<th>Number of Respondents</th>
</tr>
</thead>
<tbody>
<tr>
<td>Academia / Think tanks</td>
<td>2</td>
</tr>
<tr>
<td>Commercial comparison site / advice providers</td>
<td>3</td>
</tr>
<tr>
<td>Consumer bodies / debt advice agencies</td>
<td>10</td>
</tr>
<tr>
<td>Individual credit and store card companies</td>
<td>11</td>
</tr>
<tr>
<td>Trade Associations/ Industry bodies</td>
<td>5</td>
</tr>
<tr>
<td>Credit reference agency</td>
<td>1</td>
</tr>
<tr>
<td>Local authority</td>
<td>1</td>
</tr>
<tr>
<td>Regulatory bodies</td>
<td>2</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>35</strong></td>
</tr>
</tbody>
</table>

![Graph showing responses by sector](image)

14. This summary of responses is available electronically at [www.bis.gov.uk/creditconsultation/response](http://www.bis.gov.uk/creditconsultation/response). You may make copies of this document without seeking permission. It may be possible to make other versions of this document available on request in Braille, other languages, large fonts and other formats. Contact the Departmental contact below for information:

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Tel: 0845-015 0010
Nature of UK Credit and Store Card Market

Introduction

15. In our consultation document, we asked respondents to submit evidence about the current nature of the UK credit and store card market, focusing particularly on the incidence of multiple credit card use, the use of personal credit cards by SMEs, consumer experience of using credit cards and the profitability of credit card lending. (Q1)

Summary of Responses

16. Many organisations provided detailed evidence of market conditions in the UK at the moment. The UK Cards Association in particular supplied a great deal of data, drawing on a study by Argus Information and Advisory Services drawing on data covering almost all UK credit card accounts for the last two years and evidence collated directly from their members. We are grateful for all these submissions as they have helped us to build up a more complete picture of the current state of the UK credit and store card market. A detailed analysis of the UK credit and store card market can be found in the updated Economic Impact Assessment for the credit and store card review at www.bis.gov.uk/creditconsultation/response.
Allocation of payments

Introduction

17. General industry practice is for the most expensive debts held on a credit card to be paid off last, with the cheapest paid off first. This means that the debts attracting the highest level of interest payments (usually cash advances) will not begin to be paid off until any balances attracting a lower rate of interest (for example, those arising from a 0% balance transfer deal) have been paid off in full.

18. The Government is concerned that consumers do not realise that this method of allocating payments is common practice, and may therefore not realise that debts accruing interest at a high rate will be paid off last.

19. In light of these concerns, the Government believes that further action is necessary in this area, and has proposed a number of options:

1) Do nothing beyond current legislative and regulatory activity;
2) Improve information transparency;
3) Allocate repayments proportionally to debts attracting different interest rates;
4) Allocate repayments to the most expensive debt first;
5) Allow consumers to pay off cash advances first.

20. We asked a number of questions about these five options and also asked respondents to set out which of these five options they preferred.

1. Do nothing beyond current legislative and regulatory activity

Proposal

21. Under this option, we proposed to take no further action beyond that which emerges as a result of the implementation of the Consumer Credit Directive and the publication of the OFT’s Irresponsible Lending Guidance and asked to what extent consumers were aware of this allocation of payments structure and whether this option would provide sufficient consumer protection in this area (Q2-3).

Summary of responses

22. It is very clear from the responses received from consumers that most were not aware of their allocation of payments, even those who regarded themselves to be relatively financially literate. For example, Linda said “I have no idea in what order the cardholder applies my repayments to my debts”.

9
23. Organisations working directly with consumers, such as Paymex, a debt solution provider, highlighted this lack of awareness amongst consumers when they said “in our view very few consumers understand anything about the order of payment allocation and its implications”. Money Advice Trust described the current method of allocating payments as “a complex arrangement and one that is not easily explicable to the consumer”. They referred to clients who have transferred balances to low rate or 0% credit cards, with the intention of reducing their indebtedness, only to find their plans go wrong because they do not understand how payments to the new cards were allocated. This confusion was echoed by other consumer groups, including Citizens Advice. Credit Action pointed out that the current arrangement did not confuse only vulnerable consumers, or those with low levels of financial literacy, but affected the majority of consumers.

24. This was further substantiated by research carried out on the behalf of Nationwide, the only high street provider in the UK to operate a system of allocation of payments from highest to lowest debt.¹ This showed that nearly two thirds (63%) of credit card customers still do not understand the order in which their repayments are allocated. In its online poll of 2008 British adults in October 2009, Moneysupermarket.com also found that 69% of consumers did not know that payments were allocated from cheapest to most expensive debt first.

25. This is challenged, however, by research for the UK Cards Association, which found that 59% of the consumers they questioned already knew that if they did not pay off their balance in full, most credit card providers would allocate the payment to the balance with the lowest interest first. A further 25% did not know this, but were not surprised.

26. Of those consumers who commented on this issue, nearly all made clear that retaining the status quo would be unacceptable. For example, Ian stated “my main concern is the current allocation of payments to pay off credit card debt at the lowest interest rate first. This is scandalous!” and Kathryn said “the priority of the debt in particular is a bugbear for me. I really resent being made to drag out more expensive debt on my cards”. Adrian added “With regard to the insidious way in which payments are credited to the items attracting the lowest level of interest first. This must be stopped”.

27. These views from consumers were supported by research carried out on the behalf of Nationwide.² This research showed that over half (56%) of credit card customers would be left angry, shocked or surprised if they found out that their credit card provider pays off their cheapest debt first. Furthermore, a poll carried out on the behalf of moneysupermarket.com in October 2009 showed that 85% of consumers would feel cheated, angry or confused if they knew this.

¹ Research conducted among a nationally representative sample of 2,000 respondents online, by Marketing Sciences on the behalf of Nationwide in November 2009.
² Research conducted among a nationally representative sample of 2,000 respondents online, by Marketing Sciences on the behalf of Nationwide in November 2009.
28. Consumer groups agreed that existing measures (including those planned under the Consumer Credit Directive) provide insufficient consumer protection. Citizens Advice summed up comments: “existing consumer protection measures have failed because they rely on consumers being able to understand complex information and take action as a result. As we have shown, this is not always possible.” This was also supported by other groups including Money Advice Trust, Citizens Advice Scotland, and Credit Action.

29. However, aside from Nationwide, most credit card lenders and store card lenders highlighted the potential negative consequences of taking action in this area. Research by Oxera for UKCA found that lenders would be likely to respond to compensate for loss of revenue caused by a reversal of payment allocation. This could include reducing the availability of balance transfer deals, increasing balance transfer fees or post-promotional APR rates, and increasing the transactions APR for promotional accounts.

30. One lender stated that “no further consumer protection is required”, over and above measures already planned. This was supported by another lender, who believed that “current and proposed legislation, together with the codes of practice, already create an environment where an informed consumer can make a choice”.

31. However, despite these views, lenders also supported the UKCA position, that while they believed there was sufficient consumer understanding of this issue, there is a popular strength of feeling that the status quo cannot remain. Qualitative research for the UKCA suggests that regardless of the way in which allocation of payments is explained, consumers see the current practice as counter-intuitive. In-depth interviews for the UKCA found that consumers saw their debt as “a single entity rather than compartmentalised and therefore feel that when they pay money this should apply equally to the whole debt”.

2. Improve information transparency

Proposal

32. Under this option, we proposed to make it more explicit to consumers that debt attracting the lowest rate of interest would be paid off first and / or to provide information on what consumers could do to improve their card use, with illustrative scenarios. We asked whether improved transparency would be sufficient for consumers, and what might be the costs (Q4-6).

Summary of responses

33. Most consumers did not specifically comment on this option, although their views on the current system of allocation of payments (see option 1 above) made it clear that their concerns were less about understanding how it works, and more about ensuring that it is changed.

34. Of the very few consumers who did comment in this area, it was to provide specific suggestions for improvements in information transparency. For
example, Sheena suggested “When credit cards are advertised they should be very clear about how much they are charging in interest for each facility – purchases, cash withdrawal and balance transfers. A short clear summary of each rate charged and how repayments are applied is not difficult!” Paul agreed with Sheena and further said “I would like to see the balance that applies to each band of interest rates”. However, one consumer (Alex) did say the following “the allocation of payments clauses are in every statement every month so I cannot see how the Government can get the message through even more”.

35. While agreeing that transparency and simplicity are important, consumer groups were in agreement that increasing transparency alone would not address consumer detriment in this area. Consumer Focus summed up comments: “In general, Consumer Focus supports the goal of greater information and transparency. However, providing more information or an explanation will not prove an effective remedy in this case.”

36. Many lenders in their responses to the consultation committed to doing more to improve understanding on the allocation of payments. The UKCA believed that further increasing transparency was strongly supported by its quantitative research, and would mean that payment allocation could remain a potential tool for competition within the cards industry and that the current wide range of deals could remain available to consumers. One lender suggested that “rather than making changes to existing payment allocation methods, there would appear to be a more compelling rationale for improving transparency measures to ensure that consumers are able to make more informed choices in relation to their usage of a credit cards.” However, while these lenders’ preferred option would be to increase transparency, there was a general acceptance that, supported by UKCA’s qualitative research, further changes would be necessary.

**3. Allocate repayments proportionally to debts attracting different interest rates**

Proposal

37. We proposed that the monthly payment made by a consumer should be used to reduce each debt incurring a different interest rate on a proportional basis. We asked respondents to let us know what they thought of this option, what might be the costs, and whether there might be a preferable way of structuring repayments (Q7-10).

Summary of responses

38. No consumers commented directly on this option. Consumer groups considered that the option of allocating payments proportionally would be confusing for consumers. Money Advice Trust pointed out that this would be a very difficult concept to explain in plain English. Citizens Advice echoed this, and said that the benefits to consumers would be minimal.
Moneysavingexpert, however, considered this option to be fairest to both consumers and the market place, and thought that lenders could implement a very simple algorithm that is easy to replicate.

39. Lenders agreed with the majority of consumer groups that this option would be confusing to consumers, and Nationwide said that significant costs would be likely to come from dealing with cardholder inquiries, who will be confused at how payments are allocated. The UKCA costed this proposal at £241m over the first 2 years.

Alternative ways of structuring repayments

40. A number of individual consumers did suggest alternative ways of restructuring repayments aside from those proposed in our consultation. The most popular alternative suggestion amongst consumers was that the allocation of payments should be prioritised by the date at which the debt was incurred. Enric was typical of those consumers making this point “I personally believe that the fairest way would be that debt is paid accordingly to the date that this debt is contracted. This would still allow the companies to make some money.” and Linda said “logically, I would have thought to clear (payments) in the order in which they accumulated on the account in the first place (oldest debt to newest debt) would be the correct way”. Adrian added “Surely, payments should be credited on the basis of the date the debit was posted to the account”. The response from the UKCA acknowledged that this option was superficially attractive, but in practice could prove more confusing for consumers.

41. Another suggestion (Ali) was “why not let the cardholder tell the bank what a payment is meant to cover?” This feature is already available from at least one provider in the US.

42. The UKCA, strongly supported by other lenders, proposed a detailed alternative option, based on the US CARD Act. This would see payments above the minimum allocated to the highest interest-rate debt first, leaving lenders the flexibility to allocate the minimum payment according to business models. They saw benefits for consumers from this option, as consumers would repay less over the term of the agreement for a shorter period of time. The exemption for the minimum payment has the effect of preserving an element of competition, and offering lenders protection against the risk of being left with borrowing at non-commercial rates. The model is sufficiently flexible to allow those lenders who choose to do so to offer completely positive allocation. This new option was costed at £248m over the first 2 years.

43. However, Nationwide did not support this model. Consumers would be further confused by having two payment allocation methods applying at any one time. This option would also penalise minimum payers (likely to be the most vulnerable) by increasing their costs and time taken to repay debt.

3 www.chaseblueprint.com
4. Allocate repayments to the most expensive debt first

Proposal

44. We proposed that the current practice of allocating payments should be reversed so that payments are allocated to the highest interest-rate debt first. We asked respondents for their views on this option and to set out what would be the costs to industry (Q11-13).

Summary of responses

45. This was by far the most popular option amongst consumers who commented on this issue. Sarah summed up the views of many when she said “the best change would be to reverse the order in which the credit company applies payments so that the most expensive debt is cleared first” and Katherine said “Paying off the most expensive debt first is a simple way of getting out of financial difficulty”. Simone further added “I think the biggest issue is the allocation of payments – pay off the most expensive first and everyone (except the banks) will benefit with lower interest added” whilst Debbie commented “The repayment hierarchy allowing companies to pay off cheapest debt is outrageous and absolutely capitalising on people’s debt. This should absolutely be reversed”.

46. These views from consumers were supported by research carried out on the behalf of Nationwide. This research showed that over two thirds (67%) of credit card holders thought that the Government should intervene and make credit card providers pay off customers’ most expensive debt first. Nationwide Executive, Chris Rhodes further commented “the results (of the research) send a clear message to the Government: consumers want them to intervene to stop this unfair practice”.

47. A very small minority of consumers noted that a reversal in the allocation of payments would have consequences. Mike, for example, noted “While it would be great if low rate balances were paid of last, the result will be that that there won’t be any low rate offers.”

48. Consumer groups also expressed broad support for this option, calling it the “simplest” “most transparent” and “most straightforward option proposed”. Citizens Advice believed that as this option did not require consumers to understand how payment allocation works, or change their behaviour in order to benefit, it would have a beneficial effect on all consumers. Moneyfacts saw this benefit particularly falling on those who use the cash withdrawal facility.

49. Moneysavingexpert was concerned that this option could have an effect on the nature of balance transfer deals being offered, and that it “risks penalising savvier borrowers at the cost of the less savvy”. However, there was some scepticism amongst other consumer groups that the consequences would be as drastic as feared. Money Advice Trust noted that lenders who currently

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4 Research conducted among a nationally representative sample of 2,000 respondents online, by Marketing Sciences on the behalf of Nationwide in November 2009.
allocate payments to the most expensive debt first are still able to offer 0% interest deals, while Citizens Advice did not believe that lenders would put themselves at a competitive disadvantage by withdrawing such deals. Nationwide also supported these arguments.

50. Some lenders confirmed the concerns raised by Moneysavingexpert. One lender said that this option would mean a reduction in the availability of promotional offers, particularly life of balance offers, which would no longer be commercially viable. Argus research for the UKCA found that purchase interest rates for promotional accounts would need to increase by up to 2.75% in order to compensate for the loss of revenue, while cash interest rates would need to increase by up to 6%. The UKCA claimed this option would cost industry £533m over the first 2 years. Research carried out for the UKCA found that whilst 44% of consumers thought a reversal of the allocation of payments was a good idea, when told that this might mean credit cards would no longer offer promotional or lower interest rates, 31% changed their mind.

5. Allow consumers to pay off cash advances first

Proposal

51. We proposed a less wide ranging option to option 4, whereby payments would be allocated to cash advances first. Once all the cash balances had been repaid, any additional payments could be allocated according to lender preferences. We asked respondents for their views on this option, its effect on consumers and what the costs might be (Q14-16).

Summary of responses

52. Consumers did not specifically comment on this option, and there was no indication from comments received or from responses that they would prefer this option to a total reversal of the allocation of payments.

53. Some consumer groups commented that this option had merits, in that it provided some protection for those consumers withdrawing cash at very high interest rates. Money Advice Trust said that “any measure that protects consumers from the consequences of taking out a cash advance is to be welcomed.” However, there was a general question of how many consumers this would actually benefit, and this option did not go far enough to address the counter-intuitive nature of payments. Citizens Advice said “Whilst this option would tackle the problem associated with high interest-bearing cash advances, it would not benefit those consumers trapped into paying high rates of interest on additional purchases they thought were covered by 0% deals. As this group of consumers makes up the largest group affected by allocating payment to cheapest debt first, we do not believe it sufficiently addresses the consumer detriment in this area.”

54. Lenders did not favour this option. The UKCA said that some consumers would repay less over the term, for a shorter period of time, but in terms of
indirect costs, some groups of consumers would pay more, (although the costs for lenders were less for this option than option d above). Nationwide did not believe balance transfer users should be excluded from any protections offered to consumers.

**Preferred Option**

55. We asked respondents to let us know which of the five options proposed in the area of the allocation of payments they preferred (Q17).

56. From responses and comments received from consumers, it was clear that all those consumers who commented on this issue thought that the current system of allocation of payments was unfair and should be changed. Indeed, of those who voted in our poll, 37% said that the issue of the allocation of payments was of the most concern to them, significantly more than the second highest issue of most concern. Many consumers were shocked that this was the way in which the system worked. Matthew was typical of those who commented when he said “The practice of paying off the lowest interest balance first is nothing more than criminal”.

57. Whilst there were a number of consumers who advocated a system whereby the oldest debt is paid first, overwhelmingly, consumers thought that the allocation of payments should be reversed so that the most expensive debt should be paid off first.

58. As stated above, consumer groups (including Citizens Advice, Consumer Focus, Which?, Money Advice Trust) were most supportive of reversing the current system, so that the most expensive debt is repaid first. This was also supported by the Lending Standards Board, LACORS and a number of local authorities. Nationwide also strongly favoured this option.

59. Lenders (other than Nationwide) expressed full support for the UKCA proposal to allocate payments above the minimum payment to the most expensive debt first, leaving lenders the flexibility to allocate the minimum payment as they saw fit.
Minimum payments

Introduction

60. The minimum payment is the minimum amount that consumers must pay each month against their outstanding balance without incurring default charges from the credit or store card lender.

61. The Government is concerned that lenders have not done enough to explain to consumers the implications of making only the minimum payment. We are also concerned that minimum payments are set at such a level that if consumers were only ever to make the minimum payment they would end up paying off debt very slowly, in some cases over decades, and paying significant amounts of interest.

62. In the consultation document, the Government proposed a number of options to address these concerns:

1) Do nothing beyond current legislative and regulatory activity;
2) Improve information transparency;
3) Set a recommended minimum payment;
4) Increase the minimum payment.

63. We asked a number of questions about these four options and also asked respondents to set out which of these four options they preferred.

1. Do nothing beyond current legislative and regulatory activity

Proposal

64. Under this option, we proposed to take no further action beyond that which emerges as a result of the implementation of the Consumer Credit Directive and asked (Q18) whether this would provide sufficient consumer protection in this area.

Summary of responses

65. Some consumers expressed concern at the suggestion that the Government should intervene in the area of minimum payments. Typical comments included “If the object of this exercise really is to provide greater protection for consumers, focus on the other recommendations”, Paul and “Whilst I agree with much of what you are doing, I am very concerned about the minimum payment proposals”, Althea.

66. The main industry players agreed with these consumers that there was little need to take further action in this area. They argued strongly that one of the
main concerns raised by Government as a justification for intervention (that customers making the minimum payment would end up paying off their debts over longer periods of time and with high levels of interest) did not in fact exist.

67. Feedback from FLA members suggested that it is not the same pool of customers who always make the minimum payment and that customers will dip in and out of making this payment, depending on their circumstances. This was confirmed by research commissioned from the UKCA which found that only 3.1% of customers made the minimum payment over 12 months ending June 2009. This figure fell to 1.3% over 24 months. This research also found that making the minimum payment did not lead to significant balance growth. Indeed, accounts that only made the minimum balance in quarter two 2008 showed comparable or higher balance attrition compared to accounts that paid greater than the minimum by quarter two 2009.

68. In contrast, the majority of organisations representing consumers thought that whilst the existing proposed regulatory measures would improve the current situation, they would not, by themselves be sufficient. Credit Action said that this option would not meet the consultations’ objective of providing a better deal for consumers. Citizens Advice Bureau argued that the OFT Guidance in its current form did not go far enough, saying that “the threat of OFT action may not be sufficient to prevent unfair business practice” and Moneyfacts Group (representing both consumers and financial institutions) said “for those customers who do not read the information or who are concentrating on short term needs, further imposed legislation may be needed to curb further increases to long term debt”. The Consumer Council, representing consumers in Northern Ireland, noted that 17% of consumers now make the minimum payment compared to 11% in 2004.5

2. Improve information transparency

Proposal

69. We proposed that the consequences of making the minimum payment should be made more explicit to consumers at the start of a credit or store card relationship and during the life of the agreement. We made a number of suggestions as to the type of information that could be included to help consumers make a more informed decision on their borrowing, including the suggestion that there should a number of illustrative scenarios setting out the impact, on time and interest costs, of making the minimum payment. We asked a number of questions (Q19-21) about what type of information might be useful to consumers, and what might be the costs of providing this information.

Summary of responses

Illustrative scenarios

70. Consumers generally welcomed the suggestion that there should be more information on their credit and store card bills. For example, Suzannah said: “I do think it’s important for people to really understand how much it’s costing them” and A few consumers confirmed our concerns that there may be little awareness of the consequences of making the minimum payment. For example, JS said “I am truly shocked at the 41 years it would take to repay a £3,000 loan by minimum payments only. This message is the most powerful deterrent I have heard”.

71. Many consumers confirmed our view that it would be helpful for credit and store card statements to provide illustrative scenarios setting how much it will cost, and how long it will take, to repay the outstanding balance if only the minimum payment is made. Nadine said that this kind of information “might help people put their debt into context” and Ann added “short, large, bold print indication of how long it will take to pay off the debt with minimum payments should be mandatory” and PB further suggested this should be supplemented by “the amount of interest which would be paid and further estimates [for the estimated time to pay off a debt] for increments of (say) £10 or £20 per month”.

72. Nearly all consumer groups who responded to the consultation thought that improved information transparency measures would be helpful. The Money Advice Trust and Credit Action thought that illustrative scenarios on monthly statements showing the implications of making the minimum payment and other payment amounts would put consumers in a better position to make informed choices on their borrowing and might encourage them to pay more than the minimum. Which? agreed that providing specific information on minimum payments would be a sensible measure. Moneysavingexpert made specific suggestions for what these illustrative scenarios could say, suggesting that they should “include a strong warning to say in a large, prominent font: ‘If you make the minimum payment on this card, at the current interest rate and current balance, it will take you x years to pay off in full and cost £y in interest’”.

73. Despite their support for additional information transparency provisions, many consumer groups did not think that action here would be sufficient. Citizens Advice Scotland was typical when it said “while increasing transparency regarding the cost of credit is desirable, it will not necessarily encourage higher payments” and Citizens Advice Bureau added that “it did not believe that improving information transparency alone will resolve the problems caused by low minimum repayments”.

74. In contrast, lenders were unconvinced that illustrative scenarios would be useful in influencing consumer behaviour. They argued that this kind of additional information would only be of interest to those consumers who were not making a conscious and rational decision to pay the minimum and who therefore had the option of changing their behaviour. This group, as a
proportion both of total customers, and also total minimum payers, they argued was very small. Research carried out on the behalf of UKCA showed that when asked why they made the minimum payment, 56% of consumers said it was all they could afford, 24% said it was because they had more expensive debt elsewhere and 15% said they were on a promotional rate.

75. A number of lenders further argued that providing tailored illustrative scenarios to customers would have little basis in reality as these scenarios assume no further purchases on the card. In addition, although some lenders could see merit in the suggestion for better information, they argued that the complexity of the changes required to system development and IT in providing tailored illustrative scenarios would be costly.

Other information ideas

76. Some consumers suggested ways in which lenders could be more helpful in their dealings with consumers, aside from just simple information provision and illustrative scenarios on the credit or store card statement.

77. One suggestion for change was made by Graham who said “If people are only paying the minimum that is a clear statement that the credit card holder is experiencing a problem, the credit card companies should contact and speak to anyone who has paid the minimum for more than 6 months as a statutory obligation”.

78. This idea was separately suggested by a number of organisations responding to the consultation. One store card provider in the UK thought that it might be useful “if a borrower pays only the minimum payment for 6 months, then a letter or telephone call is made to the customer to provide information on the time it will take to clear the debt if they continue paying at this rate”. The Consumer Credit Counselling Service thought that where lenders notice habitual minimum payments, “it would be appropriate for them to contact these customers and suggest that they may benefit from a charitable debt counselling session”. The Lending Standards Board argued that regularly making minimum payments should act as a prompt to the lender to consider if a customer may be in financial difficulties and to engage in discussions with them.

79. In their response to the consultation, the UKCA, speaking on the behalf of all major lenders, proposed that credit card lenders should “separately contact habitual minimum payers every 6 months to bring to their attention the implications of adopting such a practice”. It was their strong view that such targeted intervention for the most vulnerable consumers making regular minimum payments would be most effective in encouraging a change in behaviour. One lender wondered whether it might be more appropriate to provide more detailed information on minimum payments only to those customers who had made a minimum payment in the previous month.
**Payment by direct debit**

80. A large number of consumers also suggested that it should be possible to choose how much of the credit or store card bill to pay by direct debit other than just the minimum payment or the full amount. Jan commented “if paying by direct debit, the customer has to choose between the minimum amount and clearing the entire balance each month. I am sure that lender’s systems could cope with a fixed amount direct debit; why isn’t it offered?” Gordon said “I have tried with several credit card companies to set up direct debits that are more than the minimum but they always refuse”.

81. Most of the consumers who raised their concerns about this issue suggested that there should be an option for a direct debit or standing order of an amount other than the minimum or the full amount. John thought that “all online payment sites should show three options “minimum amount”, “full amount due” or “other amount”, with none of them being pre-selected”, arguing that the practice of some lenders to pre-select the minimum payment option did not give consumers the opportunity to consider what repayment they would like to make. Neill added “consumers should have the right to choose the direct debit percentage to pay off their cards. Many card companies make this surprisingly difficult and/or difficult to manage”.

82. A greater choice in direct debit payment options was supported by a number of organisations responding to the consultation including the Money Advice Trust who said “we are aware of it being common practice for lenders to refuse requests to pay more than the minimum payment via direct debit. These restrictions should be removed” and moneysupermarket.com said “we believe customers should be given the choice of setting up direct debits for… any other amount – although this should be flexible so a customer can meet at least their minimum obligations should the pre-arranged payment be insufficient”. This was also advocated by the LACORS who argued that customers should be offered a third option of paying an amount of their choice by direct debit as well as the minimum and full amount. Moneysavingexpert also noted “it is worth noting some providers make this [the option to repay the balance in full] a bureaucratically difficult system to set up – missing it off direct debit forms”.

83. Some lenders also acknowledged that more could be done to provide more flexible payment options for consumers and a few noted that they already provide more varied payment options.

**3. Set a recommended minimum payment**

Proposal

84. We proposed that a recommended minimum payment could be set at a level which is higher than the contractual minimum payment and which allows consumers to pay off the card over a much shorter, more reasonable period of time, probably around 3 years. Consumers could be encouraged to make the recommended minimum payment through better information and easier
payment options. We asked respondents to let us know what they thought of this option and any costs and unintended consequences that might arise as a result (Q22-25).

Summary of responses

85. Many consumers liked this option, and although the majority of consumers would like us to take no action in the area of minimum payments, this was their preferred interventionary option. Some typical comments include from CB “I am in agreement with other commenters who believe that Option 3 (to set a recommended minimum) would be the sensible option” and Rebecca, who said “I think that mandating card companies to include ‘recommended payment’ options calculated to clear the card in 3 years is important”.

86. However, of those consumers who commented on this option, the vast majority made clear that they would only support a recommended minimum payment option if it was truly a voluntary payment. For example, Felicity said “I am in favour of Option 3, as long as it really is voluntary and it is possible to continue making minimum payments at the current level”. Becky added “This way people have the option of paying either the minimum or the recommended amount, empowering people to take responsibility for their own finances”.

87. A number of consumer groups supported the option of a voluntary recommended payment. Which? was supportive of introducing a time period within which outstanding balances should be repaid. The Money Advice Trust thought that consumers could be offered a range of recommended minimum payments with each allowing repayments over different periods of time leaving it for the consumer to select their favoured option and to change it as their circumstances altered. Like many consumers, the Money Advice Trust thought that a recommended minimum payment should be voluntary “no one can predict when they may have a change of circumstances or an unexpected expense that would mean they would not wish to make the higher payments temporarily or permanently”. Citizens Advice Scotland agreed saying a mandatory direct debit at a higher repayment amount “would put vulnerable clients in a situation where they are unable to meet repayment obligations”. Moneysavingexpert suggested that a recommended minimum payment to clear the card in 3 years should be one of a number of options (with minimum payment, a fixed monthly amount determined by the consumer and full repayment) provided to consumers. These four payment options should be clearly set out when the card is issued, in each monthly statement and annually.

88. However, the majority of lenders, and some other stakeholders who responded to the consultation, were worried about the practicalities of a recommended minimum payment. A number of specific concerns were raised relating to the impact of this option on consumer behaviour.

89. The UKCA, supported by many lenders, was worried that having both a recommended and contractual minimum payment “would simply be confusing for consumers and be unworkable”. This would have a knock on effect on
lenders would have to deal with the confusion, questions and complaints that they believe a recommended minimum payment would generate. This view was also supported by the Lending Standards Board and the British Retail Consortium who argued that “introducing a recommended minimum payment would be very confusing for all customers”.

90. There was also a view that as well as generating confusion, this option would do little to change consumer behaviour. Moneyfacts Group succinctly spelled this out when they said “given the number of customers who pay off their balances off in full not being affected and the customers who are causing the most concern not being inclined to pay more or unable to, the effect is likely to be limited”.

91. The UKCA and some other respondents to the consultation, including Moneyfacts Group, also noted that it was possible that setting a recommended minimum payment might actually have the opposite effect to that desired by Government. It may have the effect of reducing the amount that customers will pay back as they may think the recommended payment amount is better than their existing, higher payment. Professor Stewart and colleagues at the University of Warwick also argued that a recommended payment would be likely to raise the possibility of part repayment as a credible alternative to full repayment and that this could reduce the proportion of card holders making full repayments.

92. In addition, a recommended minimum payment may have the effect of encouraging customers to pay the higher recommended minimum when in fact they would have been better placed servicing other, more expensive, debts therefore leaving them worse off overall financially.

93. Most individual consumers did not comment specifically on the proposed 3 year time limit for the recommended minimum payment. Of those consumers who did, it was to suggest that 3 years might be too short, although none of those who commented thought it should be above 5 years. For example, PK said “If it takes 40 years to pay off credit card debt using minimum payments, why the rush to pay it off in 3 years. For large outstanding balances, 5 years (similar to many large loans) would seem perfectly adequate”.

94. A few lenders were wary of linking the recommended minimum payment to a repayment period regardless of the time period itself. They argued that this would be extremely complex given the open-ended nature of credit card borrowing. The repayment figure quoted would need to be accompanied by warnings on its accuracy and would lead to further confusion for consumers and make it harder for them to make informed choices about their debt repayment.
4. Increase the minimum payment

Proposal

95. We proposed that the minimum payment could increase thereby ensuring an earlier repayment of the balance over a shorter period of time, with lower levels of interest. We asked respondents to let us know what they thought of this option, how it might affect consumers, whether it should apply to all consumers and what might be the costs and unintended consequences that might arise (Q26-31).

Summary of responses

Disadvantages of increasing the minimum payment

96. Of all the options presented in our consultation, this was the one that attracted the most comments from consumers with hundreds of individuals commenting on this option both on our website, and more widely in other online forums.

97. Consumers were overwhelmingly against this option. Typical comments included Jeremy “minimum payments on existing accounts should not be raised as this will push many people into serious financial difficulty” and Matthew “increasing minimum payments would be suicidal and most hurt the consumers the legislation should be helping”.

98. Most consumers were worried that increasing minimum payments would push them over the edge e.g. Ray “if you force the companies to up the minimum % to pay each month then my family will be out on the street within 6 months” and Laura who said “increasing the minimum repayment will result in more and more people defaulting on their payments – surely a win for credit card companies as they will be the ones charging a fee”.

99. Some consumer groups were also concerned about the proposal to increase the minimum payment. The Consumer Credit Counselling Service, for example, worried that this could “tip a considerable number of people over the edge from manageable into unmanageable debt”.

100. Many lenders agreed with this view arguing that an increase in minimum payments would increase the probability of customers missing payments, putting these customers in default and negatively affecting their credit score. The UKCA’s research showed that of those who make a minimum payment, 56% say they do so because the minimum payment is all they can afford and concluded that “increasing the minimum payment is likely to create exactly the kind of financial difficulties that BIS is keen to avoid”. Separate consumer research carried out by TNS-BMRB corroborated this with 37% of those asked who were making the minimum payment stating that they were doing so for affordability reasons.
101. Analysis carried out by Argus on behalf of UKCA modelled the effect of increases in minimum payments on customers with different risk profiles and different utilisation rites. This analysis showed that increasing the minimum payment to 5% would affect nearly 40% (39.7%) of accounts and, on average, the typical cardholder would have to find an extra £99.65 each month to meet the increased minimum payment. Consumer research carried out by GfK NOP confirmed this analysis that higher minimum payments would affect many customers. For those consumers who make the minimum payment, an increase in the repayment rate would lead to difficulty with 10% of minimum payers already incurring difficulties in meeting the minimum payment, and a further 51% saying that they might or would definitely find it difficult to meet increased minimum repayments. The UKCA also noted the effect that different increases in minimum payment would have on their revenue with their estimates showing that the financial impact on the industry increases by roughly £400m - £450m with each 1% increase in the minimum payment.

102. A number of consumers thought that it was not for the Government to prescribe how much consumers should pay back and that they should be able to make that decision themselves. For example, Ray said “Your suggestion takes away choice, for no good reason, and will hurt vulnerable people” and this view was supported by moneysupermarket.com which said “we don’t support a mandatory increase in minimum payments – consumers should be empowered to manage their own finances”.

103. Some consumers persuasively made the case that this option would leave them worse off by preventing them from taking advantage of 0% deals and/or from paying off their most expensive card first. Samantha noted that “For me, raising the minimum payment on all my cards would result in a more expensive and longer debt repayment overall as I would be paying more money off the low interest rate cards each month (and so less off the higher rated cards)” and Tim added “what about people who make the rational decision to take advantage of low rate balance transfers? Having to repay a debt at a faster rate is penalizing them for their prudence”. Moneysavingexpert also identified this as an adverse consequence of raising the minimum payment saying “the correct repayment method to clear debts most quickly is to make just the minimum repayment on the cheaper cards and focus all spare cash on repaying the card with the highest [interest] rate”. As did the UKCA, who noted that increasing minimum payments would reduce the financial benefit for those consumers on a promotional rate. These views were confirmed by two separate pieces of consumer research which showed that a significant proportion of customers pay the minimum because they have more expensive debt elsewhere (24% according to GfK NOP and 17% according to TNS-BMRB research) or because they are taking advantage of promotional rates (15% according to GfK NOP and 13% according to TNS-BMRB).

104. Professor Neil Stewart and colleagues at the University of Warwick counselled against an increase in minimum payments because of the effect an increase would have on customers making full payments or partial payments on their credit and store cards. They stated “in an analysis of the credit card statements of 126,000 credit card holders, we find higher minimum payments are associated with fewer full repayments, with more and smaller part
repayments, and with more minimum repayments. We caution against mandating an increase in minimum payments”. They set out that whilst a higher minimum payment might help the small number of regular minimum payers in the long term, a much larger proportion of card holders may end up making lower payments and paying more interest as a result.

Benefits of increasing the minimum payment

105. A very small minority of consumers did recognise that there could be some benefits in increasing minimum payments. For example, one consumer commenting on moneysupermarket.com said “Yikes, I’d always thought that the minimum repayment was 5%, which struck me as absurdly low. If it’s actually 2-3% then it’s unbelievable that such a low rate is actually permissible” and Katherine added “Paying a higher minimum, designed to clear debts, not just service them, will also keep people out of difficulty” and Simon said “I think it’s appalling that by having such low minimum repayments; credit companies are able to keep people in virtually perpetual debt. If the repayments only cover a little more than the interest, how can someone that isn’t financially engaged ever hope to repay the capital?”

106. A few consumers further recognised that increased minimum payments would benefit consumers in the longer term. For example, Anthea said “One of my credit card lenders has increased their minimum payment to 5% and while this was a struggle in the first month I am much better off now I have budgeted for this and find my debt is decreasing at a much better rate”. A survey of 300 insolvency practitioners by the Association of Business Recovery Professionals supported this view when it found that 79% of these practitioners thought that an increase in minimum payment would encourage people to see store credit cards as short term credit rather than a long term way of life. Consumer research carried out by TNS-BMRB confirmed that a significant proportion of consumers do view credit cards as long term borrowing products. It showed that whilst the majority of customers who make minimum payments do so for less than a year, a significant proportion have been doing so for many years. Of those consumers who say they make regular minimum payments, 48% had been doing so regularly for over 1 year, and 12% of these said they had done so for over 5 years.

107. Many consumer groups, including Citizens Advice, Which?, the Money Advice Trust and the Consumer Council, agreed that minimum payments needed to increase but had a number of caveats as to how this should be implemented (see paragraph 111 below).

Implementing an increase in minimum payment

108. Of those consumers who commented on how we might implement an increase in minimum payments, nearly all asked that this should not be applied to existing debt, but should be applied to new cards only, or phased in over a period of years. For example, Enric said “this should only apply to new business, or as soon as a person has cleared off their debt, it then automatically applies for any new debt on that same card” and Steve commented that “Perhaps this (should be) phased over a number of years so
that minimum repayments in 2010 could go no lower than 2%, then 3% in 2011, 4% in 2012 and returning to what used to be the standard 5% by 2013”.

109. In the main, consumer groups agreed although there were differences in views as to how the implementation should take place and at what level the minimum payment should be set. The Money Advice Trust thought that the minimum payment could be set at 5% for new cards and new agreements with consumers with existing debt given the option to pay higher recommended minimum payments instead. Citizens Advice Scotland also thought that any higher minimum payments should only apply to new credit card accounts and the Financial Services Consumer Panel said “whilst we would like to see the minimum payment increased on new borrowing, customers must be offered the option of opting out of the higher repayment level on existing borrowing”. This view was supported by the Consumer Council, who although they advocated minimum payment levels of up to 10%, also argued that this should be for new customers only and by Which? who said that whilst they supported an increase in the minimum payment, this should be structured in a way that avoids causing additional difficulties for customers struggling to make their repayments. Moneysavingexpert thought that “the monthly payment should always cover the cost of a month’s interest, plus any fees or insurance”.

110. The majority of lenders thought that an increase in minimum payments would not be in the best interest of consumers and furthermore argued that there would be significant costs for industry in an increase. Their estimates showed that each 1% increase in minimum payment would impact industry revenue by approximately £400m to £450m. However, in their response to the consultation, a number of US lenders with a base in the UK set out how they had recently increased their minimum payments to cover interest plus fees plus charges plus 1% of the balance. They said they would support a similar increase for new accounts across the rest of the industry. Analysis carried out by Argus showed that the cost to industry of this option would be around £343m exclusive of the systems costs of moving to this method of calculating minimum payments.

111. However, Paymex, an organisation representing consumers in debt, thought that an increase in minimum payment to 5% should apply to both new and existing credit and store cards, stating: “whilst we understand this will increase the number of customers in difficulty in the short term, we believe that this problem cannot be solved unless customers who only ever make the minimum payment face up to their debt situation”. This view was supported by the Citizens Advice Bureau who said that although an increase in minimum payments should apply initially to new card accounts, “we feel strongly that increased minimum payments should eventually apply to all credit card holders... we therefore recommend that the increase is phased in for existing card holders over a few years”. Consumer Focus also strongly advocated an increase in minimum payments to all consumers, initially to 5% but possibly increasing up to 10% or 15% in the future, with some mechanisms set in place to protect those most vulnerable. These included allowing consumers to opt out of the increased minimum payment levels and to trial the increase for a 12 month period.
112. The UKCA argued that even a phased approach to an increase in minimum payment would be damaging to consumers saying “given the magnitude of even the average increase in payment that would be required, it is difficult to see how even a staggered change would mitigate the impact for a larger number of consumers rather than simply delay it”. One or two lenders further argued that an increase in the minimum payment which applied only to new debt could have the effect of reducing the amount of switching in the market and therefore have an impact on competitive behaviours. Customers with existing credit cards might find it more difficult to switch to new credit cards because they would not be able to afford the new, higher minimum payment which would apply.

Preferred Option

113. We asked respondents to let us know which of the four options proposed in the area of minimum payments they preferred (Q32).

114. Comments received from respondents to the consultation show some clear preferences in this area. Individual consumers were nearly all vehemently against an increase in minimum payment most particularly when it applied to existing debt. Some liked the recommended payment option, but only as long as it is voluntary. Most individual consumers would like to see no changes at all to minimum payment policy, although a significant minority would be interested in better information provision, and more choice in payment options, particularly for direct debit payments.

115. Lenders in the main agreed with individual consumers that there should be no increase in minimum payments on existing debt, arguing persuasively, and with supporting research and evidence, that this would lead to significant detriment to a large number of consumers who currently make minimum payments or who would struggle to do so if there were an increase. They were also unconvinced by a phased increase in minimum payment or one which would apply only to new debt. The negative effect of an increase in minimum payment on consumers who make full or part repayments was also supported by independent research from Professor Stewart and colleagues at the University of Warwick. Lenders were also wary of the confusion that is likely to be generated by a recommended minimum payment and could not see the additional value of this option. Many lenders acknowledged that more could be done to improve information for those consumers who make minimum payments, or who are at risk of doing so, and proposed specific targeted information measures to help these consumers.

116. The views of consumer groups were more varied. Pretty much all consumer groups thought that better information provision on minimum payment options would be a good thing. Many supported the idea of illustrative scenarios. However, consumer groups were more or less split down the middle in their views on options 3 and 4. Some consumer groups (for example the Money Advice Trust, Moneyfacts Group and Credit Action) were most taken with option 3 to put in place a recommended payment. Others (for example Citizens Advice, the Financial Services Consumer Panel and the Consumer Council)
wanted to see an increase in minimum payment as long as it was phased and/or applied to new debt thereby minimising harm and distress to the more vulnerable consumers. Only one or two organisations called for a blanket increase in minimum payment.

117. In conclusion, responses from the consultation show that the preferred option overall would be for improved information (option 2) with varying views on what might be the best information to provide, when to provide it and at whom it should be targeted. Many respondents across all three main groups (consumers, consumer groups and industry players) mentioned the need for more flexibility on payment amounts and mechanisms. Whilst option 3, the recommended minimum payment option, was liked by some consumers and consumer groups, there was little evidence that it would change consumer behaviour any more than better information, or indeed that it would benefit them at all. Option 4, to increase the minimum payment, was clearly contentious, with individual consumers and lenders against an increase if it applied to existing debt. However, many consumer groups could see the benefits of a phased and/or managed increase in minimum payments.
Unsolicited limit increases

Introduction

118. It is standard practice for credit and store card companies to grant their customers higher credit limits on an unsolicited basis, that is, without the customer having requested an increase.

119. In our consultation, the Government expressed concern that consumers do not have enough control over increases in their credit and store card limits. Consumers have a lack of consumer information and control over the timing and scale of limit increases, some will have low financial capability, and some may find it difficult to reject an increase.

120. In light of these concerns, the Government set out the view that further action is necessary in this area, and proposed a number of options for consultation:

1) Do nothing beyond current legislative and regulatory activity;
2) Improve information transparency;
3) Limit the size and / or frequency of individual limit increases;
4) Ban all unsolicited limit increases;
5) Allow consumers to opt in to receive unsolicited limit increases.

121. We asked a number of questions about these five options and also asked respondents to set out which of these five options they preferred.

1. Do nothing beyond current legislative and regulatory activity

Proposal

122. Under this option, we proposed to take no further action beyond that which emerges as a result of the implementation of the Consumer Credit Directive and the OFT’s Irresponsible Lending Guidance and asked (Q33-34) whether this would provide sufficient consumer protection in this area and to what extent unsolicited credit limit increases were associated with financial difficulties.

Summary of responses

123. There was quite a strong view amongst many individual consumers who responded directly that we should not interfere in this area. For example, Daniel said “the process should remain as it is. Statements clearly state that all you need to do is contact them to opt out of increases or to reduce the limits”. Mark further added “Don’t mind too much about credit limit increases, they don’t encourage me to spend more”.

30
124. Very few consumers commented on the impact of unsolicited credit limit increases on their financial situation, although Gordon said “credit limit getting increased without asking: this is wrong, wrong, wrong. For years they have been doing this with mine… unfortunately I have been tempted at times and am now in terrible trouble”.

125. Organisations dealing with consumers in debt, such as Paymex, thought that there was a clear link between financial difficulties and unsolicited credit limit increases: “we see all too many cases where customers already in severe financial difficulty are provided with unsolicited limit increases”. Citizens Advice cited cases of consumers already in difficulties or in receipt of benefits who had been granted unsolicited limit increases which had compounded their situation. CCCS agreed that this had also been the experience of clients with extreme debt in the past. However, they felt that the recession, combined with changes in lender practices, had made it much less likely that borrowers will be offered limit increases which prove unsustainable. They felt that new best practice standards were broadly sufficient but should be carefully monitored. In addition, they felt that lenders should pay careful attention to the payment patterns of consumers who actively requested limit increases and should not give unsolicited limit increases to borrowers who habitually make the minimum payment.

126. Aside from CCCS, consumer groups and debt advice agencies in general considered it unlikely that OFT Guidance would have an impact that was sufficient to change the outcome for consumers. Which? cited research it conducted in November 2009 in which 82% of respondents agreed with the statement that increasing limits without consent tempts the card holder into more debt. This view was supported by Credit Action who felt that this option would not go far enough in requiring consumers to positively engage with their lenders.

127. Industry noted that credit limit increases were used by lenders for two broad purposes. First, to enable a “low and grow” approach to lending whereby high risk customers about whom firms have only limited information can demonstrate their ability to manage increasing amounts of credit over time in a gradual and responsible way. Second, unsolicited limit increases are used to encourage people to spend on their card, either by using that card in preference to a different card, or in preference to a different payment method, or to transfer debt currently held elsewhere. Their evidence showed that balances do rise in the months following a credit limit increase by around 10-15% compared to similar accounts that did not receive an increase. This, in industry’s view, is perfectly legitimate: seeking to increase the profitability of their customers is the fundamental motivation of any business. Moreover, their evidence suggested that consumers do generally limit their own spending. Customers receiving a limit increase were likely to spend more in the month following the increase, but thereafter would spend less than they had been doing previously. This suggests that consumers use a higher limit to bring forward future spending, but do not sustain these higher spending levels.
128. Industry strongly contested the view that there is any link between unsolicited credit limit increases and over-indebtedness. The UKCA and individual lenders presented evidence that default rates are generally higher for accounts where a consumer has requested a limit increase than accounts where a limit increase has been granted on an unsolicited basis, and that accounts that receive unsolicited limit increases are actually less likely to go into default than the average account. Industry respondents also emphasised that continuous development in underwriting processes coupled with new voluntary Lending Code requirements to conduct credit checks using all available data before offering a higher limit had increased protections against over-indebtedness. Many drew attention to the fact that the Consumer Credit Directive would create a new legal requirement to conduct credit checks before offering a higher credit limit. Industry also argued that reforms to capital adequacy rules in the second Basel Accord (“Basel II”) had made it more expensive to offer consumers higher limits than they are likely to use, thereby “curbing any previous tendencies to set excessive credit limits”.

129. Industry also presented evidence that unsolicited credit limit increases are not a matter of significant concern to consumers. Data from 13 credit card companies representing 96% of the market showed that 0.05% of customer complaints between January and October 2009 were about unsolicited limit increases. There were 38 times more complaints about credit limit decreases. Consumer research supported this view. Research by GfK NOP for the UKCA found that 23% of consumers who had had their limit increased without requesting it in the last two years felt it was a positive thing, 51% were neutral and 23% thought it was negative. TNS-BMRB research found 84% of consumers said that the unsolicited credit limit increase had no effect and was not important to them. Their qualitative research, however, found that consumers were sceptical about the motives of credit and store card companies offering credit limit increases without being asked and favoured banning unsolicited increases.

130. All industry respondents emphasised that a change to current practice would be likely to have significant negative consequences, which is discussed in more detail under Options 4 and 5 below. The CBI emphasised that it would not wish to see the “low and grow” principle undermined and stated that it would not support a restriction on unsolicited limit increases unless and until robust evidence is available that reforms are justified.

131. The UKCA did, however, agree with the Government’s objective of giving consumers greater control and therefore proposed that there should be improvements in the way unsolicited credit limit increases are carried out and the information given to consumers, and that it should be made easier for consumers to decline a higher limit or reduce their existing limit if they wish.
2. Improve information transparency

Proposal

132. We proposed that transparency measures could be introduced. Information could be sent out to consumers setting out, perhaps in a separate letter, the reasons for a credit limit increase and the consumer’s option to decline it. We asked (Q35-37) what information about credit limits would be most useful and how it could be made clearer to consumers and what might be the associated costs of providing this information.

Summary of responses

133. Very few consumers commented on this option. Indeed evidence from option 1 seemed to imply that some consumers, at least, thought that the information already provided by lenders on credit limit increases was clear and sufficient.

134. A few consumers commented that it should be as easy as possible for consumers to make changes to their credit limit, and some had views on the limitations of the current system, particularly as regards the difficulties of reducing the credit limit. For example, Simon said “maybe people should be able to reduce [their credit limit] if they want and this should be simple to do” and another consumer on the BBC Forum mentioned that he was able to increase his credit limit online, but not reduce it. Kevin added “My credit card limits keep getting put up. It is a pain to phone up and wait for the reduction to be approved! It should be my right to reduce the limit” and NL added “It should be as easy to request a reduction in your credit limit as it is to increase it…. When I attempted to reduce [my limit] I was unable to do so online and on phoning the company, I was encouraged not to reduce”. David further said “Declining increases in credit card limits should not adversely affect the holders’ credit rating”.

135. In general, consumer groups felt that providing additional information to consumers would not go far enough. Which? expressed concerns that consumers may, perhaps wrongly, assume that if they decline an unsolicited limit increase this will affect their credit score or would send a message to their lender that they feel they are not in a financial position to deal with a larger limit, or might limit their ability to request a higher limit in future. Money Advice Trust felt that a letter notifying consumers of an unsolicited increase would not go far enough, but that in any case such a letter should, as a minimum, outline why the credit limit has been increased and what measures the lender took to check that the borrower could afford the new limit. CCCS, however, favoured this option, taking the view that making it easier to decline a higher limit would be sufficient to address concerns in this area. Qualitative research by GfK NOP found support for this option among consumers, who generally favoured improved communication, alongside giving customers more choice, for example through advance notification of an increase, the opportunity to opt out and information about what the minimum payments would be if you spent up to your new credit limit.
136. In summer 2008 lenders proposed a series of voluntary measures to give people better information about limit increases and to strengthen the protections for vulnerable consumers or those who do not want to be given a higher limit. The FLA suggested that the credit and store card industry should revisit this framework with Government to secure improvements in the information provided to consumers. They noted that these improvements could be quickly added to the Lending Code in order to bring benefits to consumers more rapidly. Likewise, the Lending Standards Board argued that in the light of new research commissioned by the credit card industry which shows that credit limit increases are generally being responsibly applied, the Government should look at these proposals again, with some enhancements to improve the clarity and ease of rejecting a limit increase.

137. In its response on behalf of the credit card industry, UKCA proposed further voluntary changes to their current practices, building on their earlier proposals, to ensure people are properly notified of an increase in their limit. These included: giving consumers a separate written notification at least 30 days in advance of an increase in their limit; making it easier for consumers to respond if they do not wish to accept the new limit or would actually prefer the limit to be reduced; and clearly explaining that consumers can also choose to permanently opt out of being given unsolicited limit increases. They also agreed to make it easier for consumers to decline an increase or reduce their current limit, and made explicit commitments not to raise the limits of consumers exhibiting certain signs of financial distress. The full revised industry Statement of Principles is set out in the box on pages 35 and 36.
REVISED STATEMENT OF PRINCIPLES ON UNSOLICITED CREDIT LIMIT INCREASES – JANUARY 2010

Purpose

- This ‘statement of principles’ relates specifically to unsolicited credit limit increases. This refers to a situation where we decide that it’s appropriate to increase the credit limit on your account, as a service to you as a customer.

- The principles have been developed by the industry following discussions with the Department for Business, Innovation and Skills (BIS)

- The principles build on strong existing best practice guidance and with a number of additional commitments designed to respond positively to:
  - The difficulties faced by some consumers in the economic downturn; and
  - The need for customers to have control over their finances

Key Messages for customers

- A credit card issuer’s ability to actively manage credit limits is a key part of responsible lending, helping to ensure that you are only provided with a level of credit that you can afford to repay.

- Responsible lending does not start and end when you first apply for credit – we are committed to such practices throughout the period that you hold a credit card account with us.

- The principles are underpinned by the common industry practice to consider raising credit limits incrementally over time. Such a practice is at the heart of a responsible approach to credit limit management and is sometimes referred to as a “low & grow” approach.

- This means that you may be granted a relatively low initial credit limit and, if the card is used responsibly and the data available to us suggests that you would be able to manage a higher credit limit, it may be increased (in stages) as we learn more about your use of the credit card.

- Not all customers will have their credit limit increased, because such decisions are only taken where we are comfortable with the level of ‘risk’ associated with a customer.

The Principles

1. Where we believe that it is appropriate to increase your credit limit, we want to ensure that you have some control over this change. We believe that it is important to make your options as transparent as possible and we will make it as convenient as possible for you to act upon your choices.

To support this commitment:

a. We will provide you with a clear written notification of the change we’ve made to your credit limit (by means of a specific communication), at least 30 days in advance of the change, so that you have an opportunity to consider whether you are comfortable with such a change

b. We will give you the option (in an industry standard format) to tell us that you do not wish to accept this particular increase to your credit limit, or that you would actually prefer the credit limit to be reduced

c. We will also give you the option to tell us that you do not wish to be considered for any future credit limit increases, until you advise us otherwise

d. To enable you to act upon your choices quickly and conveniently, we will make it possible for you to reduce your credit limit, with or without the need for personal interaction with us. The latter may include via websites or an automated telephone service
e. We will provide you with a clear written notification of the change we’ve made to your credit limit (by means of a specific communication), at least 30 days in advance of the change, so that you have an opportunity to consider whether you are comfortable with such a change.

f. We will give you the option (in an industry standard format) to tell us that you do not wish to accept this particular increase to your credit limit, or that you would actually prefer the credit limit to be reduced.

g. We will also give you the option to tell us that you do not wish to be considered for any future credit limit increases, until you advise us otherwise.

h. To enable you to act upon your choices quickly and conveniently, we will make it possible for you to reduce your credit limit, with or without the need for personal interaction with us. The latter may include via websites or an automated telephone service.

i. Where you do not have access to such means, or where you prefer not to use them, we will also make it as convenient as possible for you to advise us of your preference in a number of other ways, such as by letter, e-mail and a customer service telephone number.

j. Where you wish to decline or reduce your credit limit, we commit that our staff and processes will make this as easy as possible for you.

2. **We will not increase your credit limit in the following circumstances:**

   - Where you have made 6 consecutive minimum payments (on non promotional balances).
   - Where you have failed to make the minimum contractual payment requested on the last two or more consecutive monthly statements; or
   - Where an agreed repayment plan is in place in respect of your account; or
   - Where we have been formally notified by a not-for-profit debt advice agency that you are in serious discussion with it.

3. **Before we decide that it is appropriate to increase your credit limit, we will fully assess whether we feel you will be able to manage the higher credit limit, with reference to all information available to us, which will include a comprehensive range of factors, such as information relating to:**

   - how you have managed the particular credit card account, including ‘behaviour scores’ and measures around affordability/utilisation and your payment history (such as whether you often pay the minimum payment).
   - any other credit card accounts you may hold with us, or other types of relevant lending accounts you may hold with our group of companies (e.g. current account).
   - Information provided by credit reference agencies, including variations of risk/indebtedness scores/indices and debt/income ratios.
   - Information that you have provided to us.

4. **We will ensure that our staff are able to clearly explain to you why we have increased your credit limit and the options available to you.**
3. Limit the size and / or frequency of individual limit increases

Proposal

138. Following new best practice standards on unsolicited limit increases proposed by industry in summer 2008, we proposed that more could be done to reduce further the frequency of credit limit increases. We also suggested that there could be a cap on the size of these credit limit increases to mitigate the risk of lenders offering larger increases to compensate for their lower frequency. We asked (Q38-41) whether this proposal would be sufficient to address the problems, what would be appropriate caps, and what might be the costs of this proposal.

Summary of responses

139. Of those consumers who commented on this option, many liked the suggestion that there should be a cap to the size of a credit limit increase and some further suggested that this cap should be linked to earnings and/or apply across all credit cards. For example, Steve noted “there are limits to how much you can borrow on a mortgage inline with your earnings, so why not on credit cards?” Michael, a former Citizens Advice Bureau adviser, further argued that the credit limit should apply to all cards owned by one consumer, rather than to each individual card. Tony supported this view saying “something would appear to need to be done to stop customers from holding several cards from different issuers, the total credit limits for which add up to many multiples of net (family/individual) income”.

140. Consumer groups viewed this option less favourably. Which? felt that this option did not go far enough and that there were risks it would also work against consumers if the same rules were applied to credit limit increases requested by consumers themselves, a view echoed by Money Advice Trust. Others, such as Credit Action, felt that this option did not address the real issue here as it did not give consumers greater control over their limits.

141. The UKCA felt that this option would lead to arbitrary measures and would be “neither practical to implement nor, we believe, effective in achieving a desired outcome”. This approach would significantly disadvantage highly specialised “non-prime” providers who serve the highest risk customers. These customers are typically offered a £250 initial credit limit, with an aspiration from the lender that good customers’ limits will increase over time, perhaps as often as every four months, first to £500 and eventually to a typical limit of £1,000 or more. This would represent a 400% increase in twelve months. The UKCA compared this with a high street lender that offers an initial limit of £3,000 which is increased to £4,000 after twelve months; an increase of 33%. The UKCA therefore felt that a restriction on the size and frequency of unsolicited limit increase could disproportionately affect the non-prime providers because “it is widely accepted within the industry that it is not possible to profitably offer a credit card with a £250 credit limit”. In the
UKCA’s view this option would be a real threat to the long term viability of this business model and would mean that responsible high risk customers would find it hard to get credit cards and would be likely to be forced into borrowing through home credit, pawn shops or payday lending at a higher cost or, in the worst case, illegal lenders.

4. Ban all unsolicited limit increases

Proposal

142. Under this proposal, we suggested that consumers should only be granted access to additional credit if they made a positive request for a higher credit limit. Therefore, limits would only increase where consumers had actively made a decision that they wanted to borrow more. We asked (Q42-46) whether there should be a ban on unsolicited credit limit increases, what might be the benefits and risks to consumers and what might be the costs to lenders.

Summary of responses

143. A few consumers felt strongly that there should be a ban on unsolicited credit limit increases. For example, Paola commented “automatic credit increases should be made illegal” and others commented that it should be up to the consumer to ask for a credit limit increase. Mark said: “credit limits should only be increased where requested and then risk assessed”.

144. Consumer and debt advice charities generally did not favour a total ban, preferring option 5, which would allow lenders to initiate offers of a higher limit which customers could opt in to. Citizens Advice, for example, stated that “we do not think it necessary or desirable to ban lenders from making unsolicited offers of credit increases to customers, provided that customers are required to actively agree to such offers before any increase is applied”. A number of consumer groups felt that a total ban could have negative consequences for consumers, such as restricted access to credit. The Financial Services Consumer Panel, Knowsley Financial Inclusion Forum and the Consumer Council for Northern Ireland, however, preferred an outright ban.

145. Lenders were strongly opposed to a ban on unsolicited credit limit increases. In their view, this would mean that lenders only had one choice to get right the decision about how much credit to make available. This would lead lenders to take one of two possible approaches: either offering higher limits at the outset, which would risk more consumers getting into trouble, or not offering credit at all to consumers on low incomes or who are regarded as high risk. Oxera’s economic impact analysis suggested that a ban on unsolicited credit limit increases was also likely to limit competition by limiting scope for balance transfers and disadvantaging monoline credit card companies who hold less information about prospective customers and therefore have to offer lower initial limits.
Industry’s own impact analysis suggested this policy would have resulted in a loss of revenue of around £305 million in 2009 and £354 million in 2008. These losses would either have to be absorbed by industry or passed on to consumers through higher interest rates or annual fees. If the losses in 2009 were fully recouped by charging existing customers more, this would be equivalent to 0.71% being added to interest rates or the introduction of an annual fee of £5.55 on every account (£8.74 if the fee is only charged on active accounts). Lenders might also respond by reducing costs through cutting credit limits or stopping lending altogether to some customers.

In contrast to GfK NOP’s consumer research, the qualitative research conducted by TNS-BMRB found that consumers generally favoured a total ban on credit limit increases unless consumers ask for it. Respondents felt that customers would feel greater personal responsibility for debts accrued through requested credit limit increases, and would be more in control of their debt. Consumer research conducted by GfK NOP showed that 63% of consumers surveyed thought that banning unsolicited limit increases was a good idea. However, when told that this might result in people who are currently given cards with low limits not being able to get a new credit card if they wanted one, only 35% still thought it was a good idea. If they themselves might not be able to get a new card, the proportion who thought the proposal a good idea fell to 33%. When told that the change could result in credit cards coming with an annual fee in future just 17% still thought it was a good idea.

5. Allow consumers to opt in to receive unsolicited limit increases

Proposal

Under this proposal, we suggested that consumers should be able to opt in to receiving unsolicited limit increases. This could work in two ways. Either consumers could be required to opt in to each individual offer of a higher limit or there could be a provision for consumers to opt in to unsolicited limit increases at the time they enter into their credit agreement. We asked (Q47-52) whether an opt-in model would address the problem of unsolicited credit limit increases, which of the two options respondents preferred, what might be the unintended consequences of this proposal and the costs to lenders.

Summary of responses

Some consumers indicated that they would like to have more responsibility in accepting credit limit increases, although they did not necessarily set out which of the two options they preferred. JC said “I believe the most important part of the reform must be that limits cannot be increased without written consent from the cardholder”. Gerry added “I would also like credit card companies to stop automatically increasing the amount of credit on my card. If a card company thinks I need more credit then they should consult me first, not automatically raise it”. Steve set out his preference for greater consumer control at the outset of the relationship with the lender “I believe that some
onus has to be placed on the cardholder to inform that they do not wish to receive an increase [...] Perhaps a simple tickbox on an application form which allows providers to increase the limit when they feel appropriate, with the default being that they can’t”.

150. Most consumer groups favoured this option in some form. Which? supported the option of an opt in to each individual increase, but not an opt in at the outset because consumers’ personal circumstances may change over the course of their credit agreement and it may later become inappropriate for them to receive unsolicited limit increases. Citizens’ Advice Scotland argued that there should be a requirement to opt in to being offered unsolicited limit increases at the outset of the agreement, as well as a requirement to consent to each individual increase offered by the lender. Moneysavingexpert felt that either consumers should be allowed to set a maximum ceiling to which they would be happy for their limit to be increased, or they should choose to opt in to individual offers of a higher limit. Offer letters should clearly set out the reasons why a consumer might want to decline the offer, for example if they have a high amount of credit available on other cards.

151. Money Advice Trust questioned whether an opt-in would lead to restrictions in the availability of credit cards for credit-impaired consumers. They argued that this would be minimised if lenders were still able to offer higher limits that low and grow customers could opt in to and challenged the view that industry profitability depends on increasing limits to a certain level, arguing that products aimed at this group of customers will already have an increased APR to reflect the relative risk for this market.

152. The evidence from consumer research was mixed. Some evidence appeared to suggest that consumers would choose to opt in to a higher credit limit if necessary. GfK NOP research asked consumers whether they would get in touch with their card company to accept an increase in their credit limit and, if so, how they would do so. 13% said they would do so, probably by letter, 55% by phone and 21% by email. Only 11% said they probably wouldn’t contact their bank. TNS-BMRB found 83% of consumers who had contacted their bank to ask for their limit not to be changed found it easy to do so.

153. In the main, lenders were not in favour of an opt-in model arguing strongly that the profile of customers opting in to a credit limit would be more risky. The UKCA felt consumer research indicated opt in levels would be low: 86% of consumers surveyed by GfK NOP said they would not request a limit increase themselves and 73% were satisfied with their current limit. Lenders reported that only 0.6% of consumers actually opted out of a credit limit increase between January and October 2009, suggesting consumer inertia is generally very high. In their view, this meant very few borrowers would ever opt-in and that this option would therefore have the same negative consequences as option 4. In addition, they argued that the opt-in approach would introduce additional cost, bureaucracy and inconvenience for consumers who do welcome higher limits and are used to the current model.

154. Lenders also felt that not opting in to credit limit increases at the point of application might “in itself become a risk indicator” that could result in people
being declined if they didn’t opt in. Industry also expressed the view that if the Government was to make an opt-in a legal requirement, the sanction for non-compliance would have to be carefully thought through. If a criminal sanction were imposed then this might dissuade lenders from offering an opt-in by telephone as they would have to record every telephone conversation in order to prove that they had complied. The costs of this were likely to be so high that lenders would simply not offer a telephone service.

**Preferred Option**

155. We asked respondents to let us know which of the five options proposed in the area of unsolicited credit limit increases they preferred (Q53).

156. It is fair to say that, perhaps surprisingly, of all the issues covered by this consultation, unsolicited credit limit increases attracted the least number of interest and comments from consumers. There was no clear cut view amongst consumers who responded to the review as to the preferred option in this area. Some consumers felt strongly that lenders were doing enough here and no further action was required. However, at the other end of the spectrum, a few consumers felt equally strongly that consumers should be able to request or opt-in to a credit limit increase, although there was no clear majority for either of the options to ban unsolicited credit limit increases or to ask for an opt-in. There did seem to be a view amongst some consumers that credit limits should be linked to salary and should apply across all credit cards and a number called for it to be made easier for people to decline an increase or reduce their limit.

157. Consumer groups generally favoured an opt-in approach, the majority calling for an opt-in to every individual offer of a higher limit, although some, such as Moneysavingexpert also welcomed alternatives such as allowing consumers to opt in at the outset and set a maximum ceiling above which they did not wish their limit to be increased. One clear exception was CCCS who expressed the view that current standards are broadly adequate, subject to improvements in the right to decline a higher limit. The Lending Standards Board also argued that in the light of new evidence supplied by the industry which demonstrates that unsolicited limit increases are generally only given to lower risk customers and do not lead to an increased risk of default, the Government should look again at industry proposals in this area. Some consumer bodies such as the Financial Services Consumer Panel, however, favoured a total ban.

158. Lenders overwhelmingly opposed a ban or an opt-in. UKCA and FLA members both favoured giving consumers better information about limit increases and UKCA members also said they were willing to offer new ways to make declining or reducing a credit limit easier as well as formally committing not to give limit increases to people in or at clear risk of financial difficulties. Industry challenged the Government to show that any new model for credit limit increases would lead to more responsible lending and fewer indebtedness problems than their current approach.
Re-pricing of existing debt

Introduction

159. Interest rates on credit and store cards can change over time, reflecting the fact that they are open-ended products. Lenders can change interest rates in two ways. Firstly, rates can alter as a result of changes in the cost to the lender of providing credit to all consumers and generally these rate changes would apply across a whole portfolio. Lenders can also alter interest rates in response to changes in the “risk cost” of serving a particular consumer or group of consumers because of changes in the perceived risk that those consumers will default (risk based re-pricing).

160. The Government is concerned about the continuing practice amongst credit and store card lenders of increasing interest rates on existing debt (re-pricing) without properly explaining why they are doing so. Despite recent moves by the industry to make risk based re-pricing fairer and more transparent (through a Statement of Fair Principles), we are concerned that some consumers are still being subjected to unjustifiable interest rate rises on existing debt and that re-pricing is still not sufficiently transparent.

161. In light of these concerns, the Government set out objectives for reform: to ensure that consumers with limited choices are not subjected to unfair interest rate changes, that consumers are given clear information about how and when their interest rates might change, and that this is a genuine two way street: rates should go down as well as up. In our consultation, we proposed a range of options in this area:

1) Maintain the Statement of Fair Principles;
2) Further measures to provide consumers with better information about risk based re-pricing decisions;
3) Define the factors that it would be fair for lenders to take into account when changing an individual’s price on grounds of risk;
4) Limit the size and / or frequency of existing debt re-pricing;
5) Prohibit re-pricing of existing debt.

162. We asked a number of questions about these five options and also asked respondents to set out which of these five options they preferred.

1. Maintain the Statement of Fair Principles

Proposal

163. Under this proposal, we suggested that we could maintain the status quo, with lenders continuing to voluntarily follow the Statement of Fair Principles. We also suggested that this Statement could be enhanced by placing it on a statutory footing or by extending some of the Principles to provide additional
protection. We asked (Q54-55) for evidence that consumer detriment had been reduced as a result of the Statement of Fair Principles and whether the Statement of Fair Principles should be placed on a statutory footing or extended.

Summary of responses

164. Whilst very few consumers commented directly on this option, it was clear from the number and strength of comments received on this issue, that many consumers continued to feel that interest rate re-pricing was unfair and affecting them significantly. Gemma said “voluntary rules to prevent this (unfair rate rises) need to be strengthened and mandatory”. Savealert added “we’ve already seen voluntary rules to prevent this which mean you can reject rate rises yet they’ve hardly had an impact, so the Government should strengthen them”. Adrian said “these principles are a complete waste of time unless they are made legally binding and regulated”.

165. Consumer groups generally felt that the current Statement of Principles does not go far enough to protect consumers. Which? and Money Advice Trust supported the proposal that the Statement of Principles should be put on a statutory footing as a minimum. Which? also felt that the notification period should be extended to give consumers who are in a position to switch cards the opportunity to do so. In their view, the current notification period is not long enough as the application for a new card can take several weeks. Citizens Advice had seen four cases where an interest rate increase had made contractual payments unaffordable for consumers who had not previously been in financial difficulty. They felt that the commitment in the Principles not to increase rates for those who had missed the last two payments was too narrow as it only protects those already in financial difficulty. Moneysavingexpert felt that the Statement of Principles has not had sufficient impact because the consumer education needed to make them work was lacking. They felt the Principles have the potential to empower consumers, but need to be more clearly explained and enhanced to provide additional protection. They suggested a number of improvements including improving the terminology, improved explanations of why a rate has increased, and a longer period to reject the new interest rate, but also went further and called for rate increases to be applied to new debt only.

166. The Lending Standards Board, which monitors the Statement of Principles, noted that it had recently undertaken a review of compliance that found that: two thirds of firms doing risk based pricing had reduced as well as increased rates; notifications about price increases all clearly set out that consumers had the option to opt out; and all firms gave telephone numbers and encouraged consumers to contact them to discuss any concerns. However, they said that there was a case to enhance the Principles to give better explanation and setting out more clearly the circumstances in which re-pricing can occur. They felt that such improvements could be made through the Lending Code.

167. CCCS, however, felt that there is widespread misunderstanding of how credit card interest rates are calculated. They felt that as long as creditors continue to adhere to the Statement of Principles then there is no need to take further
action. Credit Action also preferred this option, arguing that that the decrease in complaints to the Financial Ombudsman Service indicated that the Statement of Principles was working, and that it would be premature to move to other options without giving the Statement of Principles more time to embed. They also felt it would be prudent to wait to observe the impact of reform in the United States.

168. The UKCA provided a detailed explanation of the role of re-pricing in lenders’ risk models. They were keen to point out that credit card re-pricing is a “two-way street”: according to their data 10.6 million credit card accounts had their rate changed between January and October 2009, 61% of these had their rate increased, whilst 39% had it reduced. Looking more closely at data for Q2 2009, the average amount of the increase in APR terms for customers who had their rate put up was 4%, whilst the average decrease was 2.6%. After a price increase, consumers are more likely to close their account and to pay off their debt more quickly. The average cost to a typical consumer of an interest rate increase is £84 a year, with costs ranging from less than £10 more a year to more than £220 year, depending on how much of their available balance consumers use and the risk segment they are in. The UKCA also presented data that showed that in the last two years high risk accounts were more likely to receive an increase and that the size of the increase was greater the more risky an account was. However, accounts in the very highest risk band were less likely to be re-priced, reflecting the commitments in the Statement of Principles and the fact that affordability checks are likely to exclude a greater proportion of this group from re-pricing decisions. We did not receive any data on recent re-pricing of store cards.

169. The UKCA and its members favoured a combination of this option and option 2. In the first nine months of the Statement of Principles’ operation 6.4 million customers had their price increased under the new rules. The proportion of those customers who took up the opt-out was relatively low, ranging from 1% to 5% depending on the lender. They considered that the findings of their consumer research showed encouraging levels of consumer awareness of the opt out: when told that when a credit card provider increases a customer’s interest rate they must provide him or her with options, one of which is to close the account and repay the remaining balance at the existing rate of interest, 45% of cardholders surveyed said they knew this already. While use of the opt-out is relatively small, the UKCA felt that this reflected the fact that it is a new part of the landscape. They claimed that their consumer research suggests that consumers respond in a reasoned way to risk based re-pricing, choosing the option that best suits their circumstances, whether this is taking up the opt-out, ceasing to use the card, or starting to use another card instead. The UKCA concluded that their evidence shows that the Statement of Principles are working effectively and that this would continue to improve as the Principles bed-in further. They did not comment in their response on whether the Statement of Principles should be placed on a statutory footing. The FLA and its members who responded supported this position, arguing that the Statement of Principles is still bedding in, but has already delivered benefits to consumers. The CBI also favoured this option.

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6 Data from 13 issuers representing 96% of the market
2. Further measures to provide consumers with better information about risk based re-pricing decisions

Proposal

170. The Statement of Fair Principles currently states that credit card lenders will explain why an interest rate has been increased if a consumer requests this. We suggested that lenders could increase transparency by proactively providing an explanation to consumers alongside any notification of a rate change. We also thought that lenders could put in place further transparency measures such as a requirement for a standardisation of how re-pricing is communicated to consumers. We asked (Q56-59) how information on risk based re-pricing could be improved, what might be the costs, and whether increased transparency would be sufficient to address the issues.

Summary of responses

171. There were few specific comments from consumers on this option. Emma suggested that the “interest rate should be shown more clearly (perhaps in a larger font) on the front of the statement. Also this should be in both monthly and annual rate formats”. Adrian argued that “customers should be given full and clear reasons why their APR has been increased with the notification of the APR rise… All notices of APR change should be as a letter with no other subject matters” and Paul added “there is too much secrecy around the calculation of risk…the consumer should have the right to view their risk rating with a credit card provider… the reasons for change should be very clearly and specifically communicated to the consumer”. A number of consumers commented that the only information they had been given on notification of an interest rate increase was that “it was a variable rate card” and Robert said “I would like to see it made compulsory for any increases to be specifically justified. I have telephoned companies but they are very reluctant to give specific reasons”. These views were echoed by consumer groups, a number of which emphasised that they felt explanations could be improved. From the comments received from the majority of consumers and consumer groups, it was clear that they felt increased transparency provisions by themselves would not be sufficient to address concerns in this area.

172. Lenders seemed to disagree with consumers and consumer groups on this: in the main they made a case for improved transparency. The UKCA, on behalf of credit card companies proposed that a new leaflet, “Risk Based Pricing Explained”, could be developed and made available to help consumers better understand how such pricing works. However, they noted that this leaflet could not provide the highly specific explanations called for by some individual consumers, stating that “it is essential that it is recognised that the associated processes are highly sophisticated and that generic explanations cannot therefore point to precise reasons for a decision relating to a particular customer’s account”. The UKCA also suggested that the leaflet could make it clearer to consumers how the opt-out actually works, underlining that they will be expected to pay down the balance at the original rate of interest over a reasonable period, as opposed to immediately. The FLA, on behalf of store
card companies, agreed that increased transparency was enough, and should ensure that customers are fully aware of the cost of the credit and how re-pricing works in practice.

3. Define the factors that it would be fair for lenders to take into account when changing an individual’s price on grounds of risk

Proposal

173. We proposed that it could be appropriate to define the circumstances in which it would be considered fair to change an individual’s price on grounds of risk. This approach would provide greater clarity and certainty for both consumers and lenders. We asked (Q60-63) whether there should be a list of these factors, who should decide what they should be, how the list could be made flexible, and what might be the consequences of such a list.

Summary of responses

174. A few consumers supported the view that it would be helpful to set out the circumstances under which interest rate re-pricing will happen. Jeremy, for example, thought that interest rate re-pricing should be stopped unless “either a) it is in the customers’ favour or b) it is in line with base rate changes or c) the terms and conditions of the account have been repeatedly broken”.

175. Consumer groups generally favoured this approach, with many calling for a consultation on the issue. Which? called for credit card agreements to clearly state under what circumstances an individual’s price can be changed and for this information to be included in summary boxes on statements. In their view, this would require greater transparency about lenders’ risk scoring models so that consumers know how they can try and improve their score to get a lower price. They also set out their view that if a customer is not missing payments then the only grounds for changing his or her interest rate should be an increase in the base rate or LIBOR. An increase in defaults in the lender’s loan book should not lead to interest rate increases on existing debt for consumers who are making their repayments: “consumers who are complying with their credit card agreements should not have to bear the cost of firms’ incorrect risk modelling”. This was especially true because some customers may be unable to switch to another card or credit product. This view was typical of many consumer groups which responded, including the Financial Services Consumer Panel, Citizens Advice and Money Advice Trust. Which? went further, and questioned whether this sort of change in the interest rate is compliant with rules on unfair contract terms. Consumer Focus argued that card companies should only be able to base their decisions on independent evidence and consumers should be able to access and challenge their risk assessment. They also felt that firms’ re-pricing decisions should be independently audited to verify their processes.
Neither the FLA nor the UKCA commented specifically on this proposal, although credit card companies did propose a new leaflet which would help explain how risk-based pricing works in general. A number of individual lenders set out their opposition to this approach. For example, one lender noted that a list of factors would be impossible to future-proof as risky behaviours are often tied to economic trends such as housing market trends or varying levels of unemployment which change over time. In their view, defining a rigid list would be likely to result in unmanageable credit losses and a lack of flexibility to help customers who wanted to improve their account status. Another lender noted that lenders must be free to manage risk according to their own skills and risk appetite, and to compete strongly on this basis. To create a single list of factors which lenders could take into account would, in their view, remove an essential element of competition in the market.

4. Limit the size and / or frequency of existing debt re-pricing

Proposal

There are already voluntary limits on the frequency of risk-based re-pricing in the Statement of Fair Principles. We proposed that this could be expanded with a commitment that any rate increase would be no more than a certain amount and/or by would be limited in frequency. The maximum size of an increase could be a set proportion of the existing rate, or a set absolute amount. We asked (Q64-68) whether there should be limitations on the size and/or frequency of interest rate increases and what effects these might have on consumers and lenders.

Summary of responses

There were no detailed comments from consumers on the proposal to limit the frequency of interest rate re-pricing. Nor did consumers specifically address the issue of caps on interest rate re-pricing. Instead, a large number of consumers focused on their concerns with the overall high levels of interest rates and called for interest rate caps. For example, Apache noted: “there is no justification for credit companies to charge APR rates of 25%+ when the interbank lending rate is pegged to 0.5%”. Linda said: “what would really help borrowers is if the Government capped the interest rate at so many points above the Bank of England rate” and Mark added “capping the interest rate that card companies can charge above the base rate would be a sensible move”.

Consumer Focus favoured this option, which provided a balanced approach in which there are strict limits on re-pricing. In their view there are times when re-pricing could be legitimate and removing the option to re-price completely could lead to higher rates for all consumers. Moneyfacts thought this option, whilst not their preferred approach, would be “one step closer to a fairer deal for consumers”. They felt rate increases should be capped at 20% of the existing rate and no more often than once every 12 months. Others, such as Which? and Money Advice Trust, however, maintained their preference that lenders should not be able to engage in risk-based re-pricing, even within set
limits. Money Advice Trust expressed concerns that lenders would push rates up to the allowed limit without adequate justification.

180. The UKCA, in its response, argued that the Statement of Principles already contains some highly significant commitments that no price increase will be made in the first twelve months, nor more frequently than once every six months thereafter. It argued that further restrictions on the frequency of re-pricing would not be in the interests of consumers as it would undermine lenders’ ability to manage risk, leading to higher prices, especially for new customers. Lenders were similarly opposed to limits on the size of rate changes, arguing that this would be a price control which interferes with the workings of the market and would be anti-competitive, as well as hindering lenders’ ability to manage risk. One exception to this was Nationwide Building Society, which indicated it was willing to limit the frequency and scale of its book based re-pricing decisions. The FLA argued that this approach would require detailed legislative change and that a strong case for reform has not been made.

5. Prohibit re-pricing of existing debt

Proposal

181. We proposed that there could be either a complete ban on re-pricing of existing debt, or alternatively, a more specific ban on risk based re-pricing. A complete ban would mean that consumers would have certainty that their interest rate on that debt would not change at all, while a targeted ban on risk based re-pricing would give greater transparency and predictability to any change. Neither of these bans would prevent lenders from charging different rates for new debt. We asked (Q69-71) what the effects of a ban might be on consumers and lenders.

Summary of responses

182. Whilst many consumers did not directly comment on whether they preferred an outright ban, or just a ban on risk based re-pricing, it was clear from many of the comments received that there was a strong preference for the former. Matthew said “the changing of interest rates in existing debts seems to me deeply unfair. Once a contract has been signed in good faith, then to change the terms […] is immoral”. Samantha noted “I think this (interest rate re-pricing) is absolutely ridiculous and should be banned”.

183. This view was underpinned by consumer concerns that their interest rates had gone up, despite no missed payments, change in circumstances, or poor credit scoring. Rob and Sue said “we have seen our interest rate hikes from 9.9% to 27% in 24 months despite having a good credit score and never missing any payments. This cannot be justified” and Elizabeth added: “stop the credit card companies from increasing interest for no reason – I have never missed a payment or even been late with a payment, but my credit card companies have increased my interest rates from an average 15.4% a year ago to an average 26.2% now”. Scott (BBC Forum) commented “If you accept a credit
card on a 16% APR and without any real justification from you the rate is increased to 32% APR, as in my case, that is not acceptable. I have had no change in my personal circumstances to justify the increase, I am just being forced to pay for others defaulting on their loans”.

184. Paymex added that anything less than a total ban on interest rate re-pricing on existing debts would still allow lenders to impose increases but use other factors (other than risk) to justify the repricing. The Financial Services Consumer Panel also felt that increasing rates on existing debts should simply be banned. Citizens Advice, however, thought a ban should be limited to risk-based re-pricing, arguing that re-pricing as a result of increases in the base rate or the inter-bank lending rate were “wholly reasonable”. Money Advice Trust took a similar approach, arguing that a targeted ban on this sort of basis would help give consumers more confidence that their rate was not changing arbitrarily whilst mitigating the potential negative impacts of an outright ban on the re-pricing of existing debt.

185. In the main, lenders reacted very strongly against the proposal to ban the re-pricing of existing debt, both in general and on the grounds of risk. They argued that the right to manage interest rates is fundamental to the operation of a long-term open-ended credit account; the risk for lenders is that money they have already lent will not be repaid so it is vital that they retain the ability to re-price that debt.

186. The UKCA stated that a ban on the re-pricing of existing debt would have cost the industry £216 million in 2008/09 and £229 million in 2007/08. Faced with this reduction in revenue, lenders would be faced with a number of choices, including absorbing the reduction in revenue, not decreasing people’s interest rates on the grounds of risk and/or recouping lost revenue through other means such as higher rates on future borrowing and for new customers or annual fees.

187. The UKCA also quoted consumer research by GfK NOP which found that whilst 60% of consumers agreed that a ban on re-pricing on existing debt was a good idea, this fell to 26% when it was suggested that credit card interest rates would be higher in future as a result and 17% when it was suggested that this meant credit cards might also come with an annual fee in future. The UKCA also cited the economic impact analysis prepared by Oxera which found that a ban on the re-pricing of existing debt would be likely to lead to limited supply of credit to high-risk consumers as the consequences of setting the wrong price for these customers could be significant. If a ban on re-pricing was combined with restrictions on unsolicited limit increases this would be likely to stop lending to high risk consumers altogether as the option of managing that risk by offering low initial credit limits would be closed off. Such comments were supported by a number of individual card companies which responded and by the FLA, which stated that “banning debt re-pricing would fundamentally affect lenders’ financial modelling and could result in the cost of credit being increased from the outset in order to cover potential risks during the term of the revolving credit product.” They noted, as did Oxera, that good customers would lose out as they would be paying a higher interest rate.
despite the fact they were lower risk in order to cover the costs of other riskier customers.

188. Finally, the UKCA cited evidence from the United States which showed that in the last year there have been significant increases in interest rates, balance transfer fees, and annual fees, whilst it has become harder to get a new credit card and existing credit limits are increasingly being cut. Research conducted by Auriemma Consulting Group into the experience of other countries also found that the restriction on the re-pricing of existing debt introduced in the US Credit Card Accountability, Responsibility and Disclosure (CARD) Act, passed last year, was likely to have significant impact on access to credit, especially for reformed debtors and young people who have no credit record. They reported that the average approval rate for new credit cards had fallen from around 25% in 2007 to around 15% today.

**Preferred Option**

189. We asked respondents to let us know which of the five options proposed in the area of re-pricing of existing debt they preferred (Q72).

190. There was a high level of concern from consumers on interest rate re-pricing. It was clear from comments received that options 1-3 would not by themselves be sufficient to address consumer concerns in this area. It was clear that many consumers would like to see an outright ban on the re-pricing of existing debts. Many individual consumers also called for a general cap on credit card interest rates.

191. Consumer groups generally favoured an approach along the lines of option 3 – setting out clearly the circumstances in which the interest rate on existing debt can be increased. However, rather than setting out a list of acceptable reasons for risk-based re-pricing, they favoured a much narrower set of grounds for re-pricing decisions, specifically preventing this for customers who are meeting their obligations unless there is an increase in the base rate or LIBOR. Some disagreed with this consensus. Consumer Focus felt that option 4 – limiting the size and frequency of re-pricing – provided the best balance, whilst CCCS and Credit Action preferred to maintain the Statement of Principles (option 1) alongside some improvements in information (option 2).

192. Lenders overwhelmingly favoured maintaining the Statement of Principles (option 1), supplemented by better information to consumers to raise understanding of how risk based pricing works and helping consumers better understand the existing opt out (option 2).
Simplicity and Transparency

Introduction

193. The consultation document examined whether, in addition to the options for increased transparency outlined in the four areas covered by the consultation, there should be additional measures to improve the simplicity and transparency of credit and store cards.

Giving consumers better information

Proposal

194. The Government believes that more can be done to provide consumers with the information they need, in ways they find easy to understand and at a time they can make best use of it. We also think there is an opportunity to take advantage of technology to present information in ways that are tailored to the needs and preferences of individual consumers.

195. The Government proposed in the consultation document that there could be benefits in providing consumers with an annual statement about their credit and store card usage. This could be provided in the form of an annual e-statement. We asked (Q73-76) stakeholders to suggest ways in which consumers can be provided with better information. We also asked for views on the annual statement, how it could be provided and what would be the costs.

Summary of responses

196. Very few consumers commented specifically on additional measures to improve transparency. In the main, consumer groups agreed with the Government on the importance of improving the quality of information for consumers. Which? noted that “greater transparency and simplicity is vital to improving consumer outcomes”. However, many consumer groups noted that any additional information provisions should be done sensibly to avoid information overload. The Lending Standards Board thought that there were limits to how much useful information can be provided and that further information should only be introduced if it is clear that it will aid understanding by the average customer. Citizens Advice cautioned against hasty action, arguing that the priority should be to ensure that the adequate explanations provisions set out in the Consumer Credit Directive are implemented effectively.

197. The vast majority of lenders were also committed to improving the simplicity and transparency of information provided to consumers. The UKCA offered to
consider the merits of the specific transparency measures proposed in the consultation and to agree a cross industry approach. A small number of lenders provided specific examples of initiatives they have taken forward to improve customer information on their borrowing and payment behaviour.

198. However, as was the case with consumer groups, a number of industry players cautioned against information overload. The British Retail Consortium was of the view that the information transparency measures arising from the implementation of the Consumer Credit Directive would be sufficient and should be given the time to take effect before further measures are brought forward. Other industry stakeholders supported the need for careful consideration of additional transparency measures before further work is done to develop these. The CBI referred specifically to the BRE / NCC report of 2007 “Warning: too much information can harm” which showed that more information could confuse consumers rather than be helpful. Like some consumer groups, they cautioned against overburdening consumers with excessive information.

199. A small number of consumers had views on the proposal for an annual statement. A few consumers thought that the current credit and store card statements were fine. For example, Robert on the BBC forum said “I have always found credit card terms simple, fair and understandable”. Linda said “I’m sure we can work that out just by getting 12 statements together and adding it up ourselves”. In contrast, Samantha noted “I think the idea of an annual statement that shows how much you have paid in interest charges is an excellent idea to help those who are less financially educated to fully realise the implications of their current interest rate”.

200. The vast majority of consumer groups liked the proposal for an annual statement including the Consumer Council, Credit Action, the Money Advice Trust and Citizens Advice. Consumer Focus suggested that Government should look at best practice in other areas to determine what information would be best covered by the statement and, together with Which? and a few other organisations, also strongly advocated the need to test the annual statement on consumers before roll-out.

201. Many consumer groups had specific ideas on the content of the annual statement. For example, the Consumer Credit Counselling Service suggested that it should be kept as simple as possible and should show total spend, total interest paid and total still owed. Which? further suggested that the annual statement could provide information on how much customers might have saved had they paid off their card at different repayment levels. Which? and the Money Advice Trust both argued that it was important for the annual statement to provide details of sources of advice for those customers who are struggling. The Money Advice Trust further suggested that the annual statement should include details of the Moneymadeclear credit card comparison tool.

202. A number of consumer groups also had ideas for the format of the annual statement. For example, the Money Advice Trust argued that the statement should use prescribed terms and format to make it easier for customers to
compare across credit and store cards. The CCCS suggested that all annual statements should be issued in the same month as this would encourage customers to really compare their debts across multiple credit cards. Credit Action went further to argue that all credit and store cards held by the customer should be listed in the same statement. Moneyfacts Group cautioned as to how easy it would be to make meaningful comparisons between cards as the same pattern of spending would be needed on each card and it would assume no changes to terms and conditions and interest rates in the future. Many consumer groups, including Citizens Advice, CCCS and Which? also argued that the annual statement should be available in hard copy as well as online to cater for those customers who may not have ready access to the internet.

203. The UKCA made a commitment to consider the merits of an annual statement. Supporting the views of some consumer groups, they argued strongly that an annual statement should not be introduced before the content, format and usefulness has been tested on consumers. One lender pointed out that the development of the annual summaries for current account customers required a great deal of work and effort and that we would need be certain of their value to consumers before committing to roll-out.

204. A small number of industry organisations raised specific concerns about the practicalities of developing an annual statement. The British Retail Consortium and the FLA could not see what additional benefits would be gained from an annual statement given that consumers receive detailed monthly statements upon which they can base their switching decisions should they so choose. One lender argued that there was no real need for a complicated tool such as an e-statement, as it would be easier for lenders and more transparent for consumers to provide information on a paper copy which consumers could then input into a price comparison site. One store card lender explained that an annual statement would be inappropriate for store cards, as many customers only use their card occasionally and the cost of preparing such a statement would be disproportionate in relation to the benefits arising for consumers.

205. Overall, consumer groups and lenders agreed that there is always merit in improving information to consumers, but both cautioned against information overload. In the main, consumer groups liked the idea of an annual statement and had a number of ideas as to how this should be presented and what information it should include. There was some limited support from some lenders for the annual statement but a strong feeling that further discussion was needed and that it would need to be tested with consumers before any decision is made.
Simpler card lending products

Proposal

206. For some consumers, the complexity of card products presents a barrier to using the card with confidence, even allowing for better information. As a result, in our consultation document, we proposed that it may be appropriate to design a basic, cheap and accessible credit card that consumers could use with confidence. Alternatively, a benchmarking or labelling system could be developed whereby all card products would be assessed against a set of agreed standards. We asked (Q77-80) for consumer and stakeholder views on the option for a stakeholder card and / or a standardised labelling system.

Summary of responses

207. Very few consumers commented on these options for simpler card lending products. However, George supported the suggestion for a labelling system, saying “There should also be a simple way (perhaps like the food traffic lights system) whereby people can figure out which company is going to give you the best deal” as did Dora, who said “I think that labelling would be a good idea, to let you know precisely the pros and cons of any credit card” and Paul “I fully support the standardised labelling and scoring of credit cards which would make comparison far easier for consumers”. In contrast, Stephanie noted “if you are aiming to create simplicity, additional labels and systems are surely to be avoided”.

208. Few consumer groups commented specifically on the suggestion for labelling and benchmarking schemes. A number of consumer groups liked the idea in principle. For example, Credit Action supported the development of a clear labelling system and agreed that the system in place to label food was a good starting point for discussion. However, a number of other consumer groups, like the Money Advice Trust and Consumer Focus, found it difficult to see how such a system would work in practice. The Money Advice Trust argued that credit and store cards are complex products where the suitability of the card depends on the customer and on how the customer uses that card – it is difficult to see how such products would be suited to simple labelling schemes.

209. A few of the major consumer groups did not believe that labelling or benchmarking schemes went far enough in making it easier for consumers to compare credit card products. Consumer Focus would like to see lenders reduce the variability of their charges and set out more reliable APRs so the way in which consumers can accrue charges on their credit and store cards is clearer. Which? supported the need for clearer APR calculations and also wanted to see a standardisation of the calculation of interest rate charges.

210. There was limited support amongst industry for a labelling or benchmarking system. UKCA said that they would be willing to consider this further as long as such a system was consistent, reliable and not misleading to customers.
However, the UKCA and a number of lenders raised initial concerns about how useful such schemes would be to consumers.

211. Supporting the view of the Money Advice Trust, the UKCA pointed out that there are difficulties with developing a labelling system for a product such as a credit card, which is used for different purposes by different customers and even sometimes by the same customer. One credit card lender further argued that trying to simplify a complicated financial product in such a way could cause more confusion and might lead to consumers choosing a credit card which was not right for them. The Moneyfacts Group thought that the regularly changing nature of credit cards would make it difficult to develop benchmark and labelling standards that would have any longevity. Another lender further commented that a labelling system would really only be of use to those customers who carry a balance on their credit card, and the majority who use it just as a transaction means would see no advantage at all to labelling. One credit card lender also argued that it was not clear how labelling would add any more useful information to customers beyond that already provided by third party comparison websites and the FSA’s forthcoming MoneyMadeClear website.

212. Overall, although only a small number of consumers commented on labelling and benchmarking schemes, those who did, liked the idea. Both consumer groups and industry were willing to explore labelling schemes further although both expressed concerns about the practicality of such schemes: in particular, the difficulty of applying a simple label to a complex, evolving product; the usefulness of such schemes for the majority of consumers who carry no balance on their cards; and the likelihood of consumers benefiting from such schemes given other comparison methods available on the market.

213. Very few individual consumers commented specifically on the proposal for a basic credit card. GK liked the idea and said “each card issuer should be forced to include one standard basic card within the variety they offer”. However, Debbie thought that “a simple credit card won’t help. It will make less money for credit card companies so they will pay less commission for selling it and consumers who would be better off with it will simply never hear about it”.

214. There was some limited support from a number of consumer groups for a basic credit card. Citizens Advice, for example, thought that such a product would be particularly beneficial to lower income consumers, not only in improving transparency and simplicity, but also as an alternative to higher cost credit for these customers. Citizens Advice Scotland thought that “consideration should be given to introducing a basic credit card that serves the interests of low income or vulnerable clients” whilst the Consumer Credit Counselling Service thought that this could be similar in nature to a basic bank account. The Consumer Council further suggested that such a product should be developed with credit unions.

215. However, as was the case for a labelling and benchmarking scheme, whilst supporting this idea in principle, a number of consumer groups had concerns about the practicalities of developing such a product and its value to consumers. Moneyfacts Group explained the key concern succinctly when
they said that past experience has shown that stakeholder products are often less competitive and not attractive to consumers – indeed they will tend not to be the best or the cheapest card as they are likely to be designed for customers who are new to credit or have had difficulties and are therefore higher risk for the lenders. The CCCS and Which? and the Lending Standards Board all raised similar concerns arguing that the basic credit card may not in fact be the best product for a consumer. Which? was particularly cautious about the value of a basic credit card to consumers and thought that more consideration was needed before taking this idea forward.

216. The UKCA committed to look at the idea for a basic credit card further if necessary, but they, and many lenders in their specific responses, had concerns about this idea. These centred around whether such a product would be of any value to consumers given the costs of providing it. For example, one lender argued that a basic credit card assumes that consumers have standard requirements that can be met by such a product. However, this is not the case, and there are already a range of products in the market which are available to meet diverse customer needs. Another lender, echoing some of the concerns raised by consumer groups, could not see how consumers would benefit given that such a card would be likely to be priced the same or more expensively than more traditional credit cards in order for lenders to make a profit.

217. Some lenders noted that they are either developing, or considering developing, a more basic credit card product for some of their customers. They did not believe that such a product should be made mandatory. They thought that the design and elements of such a product should be left to the market to determine and lenders should have the choice to whether or not there was value in such a card. Indeed, evidence from one lender who had introduced a simple flat rate card in 2007 showed that it did not sell well (fewer than 1,000 issued).

218. Overall, the respondents to the consultation could see the potential value of a basic credit card, and this was particularly true of the consumer groups. However, there was some concerns about whether it would be possible to develop a card which would benefit consumers and whose features would be attractive to them. There was acknowledgment across the board that if a basic credit card product is to be developed, far more work is needed.
Other Issues

Education

Summary of responses

219. A number of consumers who provided comments argued that one of the most effective ways of ensuring that people do not get into problem debt would be to promote and encourage more education about these issues. For example, Pat said “young people should be taught to budget” and Lee added “it might be an idea to start teaching financial management as part of the national curriculum. Many of us have been born into a culture of debt and have had to educate ourselves out of it. Not everybody is capable of doing this, so it should be taught in schools”. Msmoneywise supported this when they argued “The best solution in the long-term is to re-introduce home economics into the school curriculum - teach the young to only buy what they can afford”. The CBI also highlighted the importance of consumer education in their response to the consultation and welcomed the introduction into the school curriculum of programmes on indebtedness and financial awareness.

Store Card Selling

Summary of responses

220. A number of consumers, supported by consumer groups like Credit Action and Consumer Focus suggested that more needed to be done to improve the training of operatives who sell store cards. Credit Action noted “we have concerns that the assistants offering credit are not adequately trained in the features of the financial product they are offering” and Consumer Focus noted the potential for consumers to be drawn into products that may be available elsewhere for less cost.

221. A survey of 300 insolvency practitioners, carried out by the Association of Business Recovery Professionals found that over three quarters (76%) thought there should be a ban on the selling of store credit cards by people who are not qualified to sell financial services products at point of sale.

222. Consumer Focus further suggested that there should be a cooling off period of 14 days where consumers can reflect on whether they would like to keep the store card. On 25 January 2010, MPs also called for an amendment to the Financial Services Bill which would allow the OFT the power to cap interest rates on store cards if they prejudice the interests of debtors and would also allow a cooling off period to help stop pressure selling of store cards at checkouts.
**Regulatory Pressures**

Summary of responses

223. In their responses, a number of lenders urged the Government to consider the impact of additional regulation in an already highly regulated and difficult market. Some of the recent regulations that industry have had to comply with and which they quoted included the Consumer Credit Act 2006, the Consumer Credit Directive 2008, the Payment Services Directive 2007, the BIS Credit Card Summit 2008 and the Select Committee enquiries.

224. A number of industry organisations including the CBI and the British Retail Consortium argued that forthcoming changes, most particularly the implementation of the Consumer Credit Directive and the publication of the OFT Irresponsible Lending Guidance should be given the chance to take effect and be reviewed before any additional regulatory pressures are put in place which overlap with both of these. They argued that this was particularly true as regards improved and enhanced transparency in the areas of allocation of payments, minimum payments and the price of credit.
Annex A: List of Consultation Questions

Chapter 1: Introduction

1. The Government calls on consultees to submit evidence about the current nature of the UK credit and store cards markets, including in particular:
   - The incidence of multiple credit card use, particularly among the most indebted consumers
   - The use of personal credit cards for business purposes by the owners of small firms
   - The consumer experience of using credit cards and dealing with their lenders
   - The profitability of credit card lending and the impact of the economic downturn on both consumers and lenders.

Chapter 2: The allocation of payments

Option 1: Do nothing beyond current legislative and regulatory activity

2. We would welcome evidence on the extent of consumer understanding of the order of payment allocation and its implications.

3. Will the implementation of the Consumer Credit Directive, combined with OFT guidance, provide sufficient consumer protection in this area?

Option 2: Greater information transparency on the allocation of payments

4. How could the allocation of payments be made more transparent for consumers?

5. What effect is improved transparency likely to have on consumer behaviour? Would it sufficiently address consumer detriment?

6. What might be the cost to lenders of implementing this change? What might be the longer term cost?

Option 3: Allocate repayments proportionally to debts incurring different interest rates

7. What effect might this option have on consumers?

8. How might lenders react to a requirement to allocate repayments on a proportional basis?
9. What might be the cost to lenders of implementing this change? What might be the longer term cost?

10. Are there alternative ways of structuring repayments which would be preferable?

Option 4: Allocate repayments to the most expensive debt first

11. What effect might this option have on consumers?

12. How might lenders react to a requirement to allocate repayments to the most expensive debt first?

13. What might be the cost to lenders of implementing this change? What might be the longer term cost?

Option 5: Allow consumers to pay off cash advances first

14. What effect might this option have on consumers?

15. How might lenders react to a requirement to allow consumers to pay off cash advances first?

16. What might be the cost to lenders of implementing this change? What might be the longer term cost?

17. Of the 5 options for reform of the allocation of payments, which do you prefer?

Chapter 3: Minimum payments

Option 1: Do nothing beyond current legislative and regulatory activity

18. Will the implementation of the Consumer Credit Directive, combined with OFT guidance, provide sufficient consumer protection in this area?

Option 2: Greater information transparency on minimum payments

19. What information on minimum payments would be the most useful to consumers and how often could it be provided?

20. What effect is improved transparency likely to have on consumer behaviour? Would it sufficiently address consumer detriment?

21. What might be the costs to lenders of implementing this change? What might be the longer term cost?
Option 3: Set a recommended minimum payment

22. Should there be a recommended minimum payment?

23. How could the recommended minimum payment be set?

24. What might be the unintended consequences of a recommended minimum payment? How might it impact on consumer repayment behaviour?

25. What might be the costs to lenders of implementing this change? What might be the longer term cost?

Option 4: Increase the minimum payment

26. Should the minimum payment increase?

27. How could this increase in minimum payment be set?

28. How many consumers would be affected by an increase in the minimum payment, for example, if it were raised to 5%? How many of these consumers would be unable to meet these higher repayment levels? How many consumers holding balances on more than one credit card are likely to be affected?

29. Should an increase in the minimum payment apply to all consumers or to a subset of consumers?

30. What might be the costs to lenders of implementing this change? What might be the longer term cost?

31. What evidence do you have about the impact of previous reductions or increases in the level of minimum payments on cardholders?

32. Of the 4 options for the reform of minimum payments, which do you prefer?

Chapter 4: Unsolicited limit increases

Option 1: Do nothing beyond current legislative and regulatory activity

33. What evidence do you have that unsolicited credit limit increases are not associated with financial difficulties?

34. Will the implementation of the Consumer Credit Directive, combined with OFT Guidance, provide sufficient consumer protection in this area?
Option 2: Greater information transparency on unsolicited credit limit increases

35. How could information about credit limits be made clearer and more accessible to consumers?

36. What particular information do you think would be most effective in encouraging cardholders to be more proactive in managing their credit limit?

37. What might be the cost to lenders of implementing this change? What might be the longer term cost?

Option 3: Limits on the size and/or frequency of individual limit increases

38. Would limits on the frequency and/or size of credit limit increases be sufficient to address the issues in this area?

39. What would be appropriate limits? Who should set them?

40. Under this approach, how could consumers’ ability to request a new increase be preserved?

41. What might be the cost to lenders of implementing this change? What might be the longer term cost?

Option 4: A ban on all unsolicited limit increases

42. Do you have evidence that consumers who apply for a credit limit increase are a significantly worse credit risk than consumers that do not?

43. Should lenders be banned from offering unsolicited limit increases? Should a ban apply to all consumers?

44. What do you believe would be the benefits and risks to consumers? How severe are any risks?

45. What might be the cost to lenders of implementing this change? What might be the longer term cost?

46. How could a ban be implemented in a way which minimises unintended impacts on both consumers and lenders?

Option 5: Allow consumers to opt in to receiving unsolicited limit increases

47. To what extent do you think that an ‘opt-in’ model for credit limit increases would rectify the problems identified in relation to unsolicited credit limit increases?
48. What might be the unintended consequences of this option, including the implications for low and grow lending?

49. Should consumers be required to opt in to each individual increase or to all increases?

50. How could an opt in be implemented so that consumers would not harm their chances of getting the card they want?

51. Could a fully flexible approach be made to work?

52. What might be the cost to lenders of implementing this change? What might be the longer term cost?

53. Of the 5 options for the reform of unsolicited credit limit increases, which do you prefer?

Chapter 5: Re-pricing of existing debt

Option 1: Maintain the Statement of Principles

54. The Government would welcome further evidence of whether or not the Statement of Principles has been effective. In particular, we would welcome evidence since November 2008 of:

- Trends in re-pricing activity by lenders and the impact of the Statement of Principles on the scale and nature of re-pricing activity;
- Whether consumers are aware of their choices under the Statement of Principles and able to exercise them effectively;
- How consumers have chosen to exercise their choice following a re-price (e.g. take up of the option to pay down their balance at the existing price, take up of alternative products, switching);
- The extent to which consumers understand risk-based re-pricing and the explanations provided to them by lenders;
- Volume of complaints on re-pricing (received by lenders, consumer groups or FOS) and the nature of those complaints;

55. Should the Statement of Principles be placed on a statutory footing?

Option 2: Further measures to provide consumers with better information about risk-based re-pricing decisions

56. How could transparency on risk-based re-pricing be improved? At what stage would it be most appropriate to provide additional information (e.g. pre-contract, monthly statements, when customer requests)?

57. How could measures to improve transparency be balanced against the risk of information overload?
58. What might be the cost to lenders of implementing this change? What might be the longer term cost?

59. Do you think that increased transparency around changes to interest rates would be sufficient to address problems reported by consumers?

*Option 3: Define the factors which lenders can take into account when changing an individual’s price on grounds of risk*

60. Should there be a list of the factors that lenders can take into account when changing an individual’s price on grounds of risk?

61. Who should decide what those factors are?

62. How could such a definition be made flexible enough to adapt to future changes?

63. What are the possible unintended consequences of this approach?

*Option 4: Limit the size and frequency of interest rate increases on existing debt*

64. Should there be limitations on the size of any interest rate increase on existing debt? What should these be?

65. Should there be further limitations on the frequency of interest rate increases? What should these be?

66. What effects might these limitations have on consumers?

67. How might lenders react to these limitations?

68. What might be the cost to lenders of implementing this change? What might be the longer term cost?

*Option 5: Prohibit re-pricing of existing debt*

69. What effect might a ban on re-pricing of existing debt have on consumers?

70. How might lenders react to such a ban?

71. What might be the cost to lenders of implementing this change? What might be the longer term cost?

72. Of the 5 options for the re-pricing of debt, which do you prefer?
Chapter 6: Simplicity and Transparency

Annual e-Statement

73. The Government invites views from stakeholders on ways to give consumers better information about credit and store cards.

74. Would an annual statement be beneficial to consumers? Should it be provided to all consumers or only to a subset of consumers? What information should be included in such a statement?

75. Could such a statement be provided in a consistent, portable electronic format? What would be the costs of providing such a statement? How could we ensure that consumers without internet access also benefited?

76. How would this approach fit with the other policy options discussed?

Simpler card lending products

77. Would a “stakeholder” card lending product with basic and accessible features be beneficial to consumers? What might such a card look like?

78. What would be the costs to lenders of offering such a card?

79. Is there merit in considering a standardised labelling system for credit and store cards? Could this be taken forward on a voluntary basis pending revised EU legislation?

80. How would this approach fit with the other policy options discussed?
Annex B: List of Respondents

In addition to over 900 comments received online and by email, there were 35 formal responses to the public consultation. These are listed below, with the exception of 1 respondent who wished to remain anonymous.

American Express
Barclaycard
British Retail Consortium (BRC)
Callcredit Ltd
Capital One
Confederation of British Industry (CBI)
Citizens Advice
Citizens Advice Scotland
Consumer Credit Counselling Service (CCCS)
Consumer Focus
Credit Action
Finance and Leasing Association (FLA)
Financial Services Authority
Foundation for Information Policy Research
Home Retail Group plc
HSBC
Islington Debt Coalition
Knowsley Metropolitan Borough Council
Local Authorities Coordinators of Regulatory Services (LACORS)
Lending Standards Board
Lloyds Banking Group
MBNA – Bank of America
Money Advice Trust
Money Facts Group plc
Money SavingExpert.com
Money Supermarket.com Financial Group Ltd
Nationwide Building Society
R3
Royal Bank of Scotland (RBS)
The Consumer Council
UK Cards Association
University of Warwick
Vanquis Bank
Which?

In addition to the above named organisations 204 formal responses from individual consumers were also received. These have not been named in this list.
Annex C: List of Organisations BIS met with

- Dr Neil Stewart – 9 November 2009, 26 January 2010
- RBS – 10 November 2009
- OFT – 16 November 2009
- The FLA and a range of store card providers – 18 November 2009
- CBI Consumer Credit Working Group – 23 November 2009
- Consumer Focus – 3 December 2009
- PricewaterhouseCoopers – 9 December 2009
- UK Cards Association – 4, 16 December 2009, 23 February 2010
- Nationwide Building Society – 17 December 2009, 13 January 2010 and 17 February 2010
- Consumers Union of the United States – 5 January 2010
- US Public Interest Research Groups (PIRG) – 5 January 2010
- Consumer Federation of America – 5 January 2010
- US Department of Treasury – 5 January 2010
- Barclaycard US – 5 January 2010
- Independent Community Bankers of America – 5 January 2010
- Office of the Controller of Currency, US Department of Treasury – 5 January 2010
- Capital One Financial Corporation – 6 January 2010
- American Bankers Association – 6 January 2010
- Subcommittee on Financial Institutions and Consumer Credit, US House of Representatives – 6 January 2010
- Bank of America – 6 January 2010
- US Senate Banking, Housing and Urban Affairs Committee – 6 January 2010
- Federal Reserve Board of Governors – 6 January 2010
- Federal Reserve Bank of New York – 6 January 2010
- JP Morgan Chase Bank – 7 January 2010
- Citicards – 7 January 2010
- American Express – 7 January 2010
- Argus Information and Advisory Services – 10 February 2010
- MBNA – 10 and 17 February 2010
- Barclaycard – 10 February 2010
- Capital One – 10 and 19 February 2010
- Finance and Leasing Association – 10 and 19 February 2010
- Home Finance Group – 10 February 2010
- HSBC – 10 February 2010
- Laser UK – 10 February 2010
- Lloyds Banking Group – 10 and 19 February 2010
- Oxera – 10 February 2010
- Royal Bank of Scotland – 10 and 17 February 2010
- Santander – 10 February 2010
- UK Cards Association – 10 and 23 February 2010, 2 March 2010
- Vanquis Bank Ltd – 10 February 2010
Annex D: Glossary

Allocation of Payments: A practice whereby any credit or store card payment from a consumer is allocated to the debt incurring the lowest interest rate first.

Balance transfer deals: A balance transfer deal allows consumers to transfer some of their debts and pay the sum off at a 0% interest rate for a set period of usually between six and 14 months. After this period ends, the balance begins to attract interest.

Base Rate: This is now officially called the bank rate. It is the main interest rate in the economy, set by the Bank of England, upon which others’ rates are based.

Credit Card: A card issued by banks, retailers and other financial institutions which allows the card holder to make purchases on credit. A credit limit is established on an individual basis and interest is charged on the outstanding balance.

Credit Card Summit: This took place in November 2008 and was chaired by the Consumer Minister and attended by all key players in the credit and store card market. They agreed a statement of Fair Principles which governs how and when they will change a customer’s interest rate when their individual risk profile alters.

Credit Limit: The maximum spend a consumer can make on a credit or store card.

Credit Reference Agency: Credit reference agencies provide lenders with information about potential borrowers, which they then use to make lending decisions. The information shared may include information about borrower’s previous credit history. They hold certain information about most adults in the UK. This information is called your credit reference file or credit report.

Consumer Credit Directive: The Consumer Credit Directive is EU legislation which needs to be adopted by all EU countries by June 2010. It aims to create a common credit market across the EU and to maintain high levels of consumer protection.
| **Finance and Leasing Association:** | The Finance & Leasing Association is the leading trade association for the asset, consumer and motor finance sectors in the UK. Its members include banks, building societies, finance houses, credit and store card providers, motor finance companies and asset finance and leasing companies. |
| **Financial Ombudsman Service:** | The Financial Ombudsman Service is a public body set up by Parliament. It is the official independent expert in settling complaints between consumers and businesses providing financial services. |
| **Financial Services Authority:** | The Financial Services Authority is the main City regulator whose job is to protect investors' interests. |
| **Irresponsible Lending Guidance:** | This draft Guidance was launched for public consultation by the OFT in August 2009. The consultation closed on 21 October 2009 and the OFT expects to issue its Guidance around the end of March 2010. The final draft of the Guidance will provide guidance on lending behaviours and practices which the OFT considers to be irresponsible. |
| **Lending Code** | A voluntary code of practice which sets standards for financial institutions to follow when they are dealing with their personal and small business customers in the UK. |
| **Lending Standards Board** | The LSB is responsible for the Lending Code and helps firms to interpret and its requirements. It also monitors and enforces compliance with the Code, and identifies any gaps or deficiencies in the Code that could lead to consumer detriment. |
| **Minimum Payment:** | The minimum amount that a consumer must pay on the outstanding debt on their credit or store card. |
| **Office of Fair Trading:** | The OFT is the UK's consumer and competition authority. Its mission is to make markets work well for consumers. It is a non-ministerial Government department. |
| **Risk-based re-pricing** | This is the practice by which interest rates are altered in response to changes in the “risk
“cost” of serving a particular consumer or group of consumers because of changes in their credit score.

Self-regulation: This is the practice whereby regulation is not imposed by Government but is undertaken voluntarily by industry players in the market.

Store Card: A card issued by a retailer or group of retailers (sometimes financed by a third party lender) which only allows the card holder to make purchases on credit in certain stores. A credit limit is established on an individual basis and interest is charged on the outstanding balance.

UK Cards Association: The UK Cards Association is a trade body that gives credit, debit and charge card issuers, and merchant acquiring banks a forum where they can work together on non-competitive issues.

US CARD Act 2009 The Credit Card Accountability Responsibility and Disclosure (CARD) Act of 2009 or is a federal law passed by the United States Congress and signed by President Barack Obama on May 22, 2009. It is comprehensive credit card reform legislation that aims to establish fair and transparent practices relating to the extension of credit under an open end consumer credit plan, and for other purposes.